Supreme Ct.

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No.

In the

Supreme Court of the United States

OCTOBER TERM, 1997

NATIONAL ENVIRONMENTAL WASTE CORPORATION,

Petitioner,

v.

THE CITY OF RIVERSIDE, CALIFORNIA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the petition for certiorari should be granted to resolve the split among the Courts of Appeals regarding the proper standard for determining when an automatic stay under the Bankruptcy Code, 11 U.S.C. § 362, should be retroactively annulled?

2. Whether the petition for certiorari should be granted because the decision of the United States Court of Appeals for the Ninth Circuit to retroactively annul an automatic stay violates the plain language and intent of Bankruptcy Code § 362(d)(1) and five hundred years of equity jurisprudence where the creditor had knowledge of the bankruptcy and the debtor engaged in no egregious conduct and did not act in bad faith?

3. Whether the petition for certiorari should be granted to correct the erroneous decision of the United States Court of Appeals for the Ninth Circuit to retroactively annul the automatic stay in this case?

LIST OF PARENT COMPANIES AND SUBSIDIARIES

Pursuant to Supreme Court Rule 29.6, Petitioner, National Environmental Waste Corporation, provides the following information: The sole owner of National Environmental Waste Corporation is Samuel Cardelucci. National Environmental Waste Corporation has no subsidiaries.

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The opinion of the court of appeals (App., *infra*, A-1) is reported at 129 F.2d 1052. The opinion of the district court (App., *infra*, E-1) is unreported. The opinion of the bankruptcy court (App., *infra*, B-1) is reported at 191 B.R. 832.

JURISDICTION

The court of appeals entered an order denying the Petition for Rehearing and Suggestion for Rehearing En Banc on January 6, 1998 (App., *infra*, D-1). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 362(d)(1) of the Bankruptcy Code provides in pertinent part that "on request of a party in interest and after notice and hearing, the court shall grant relief from the stay . . . such as by terminating, annulling, modifying, or conditioning such stay for cause . . ." 11 U.S.C. § 362(d)(1).

STATEMENT

Petitioner, National Environmental Waste Corporation, a California Corporation, ("Newco") provided waste hauling services to the respondent, City of Riverside, California (the "City") since 1972. Beginning in 1991, the City was divided into five geographic areas for purposes of solid waste hauling services. The City retained four different enterprises to service those areas, including Newco. The 1991 contract between Newco and the City to provide waste handling services was an "evergreen" contract -- a contract that contained a provision for automatic renewal every year. Under the

contract, the City was given the right to cancel the contract with Newco without cause upon eight years' notice. Similar provisions were included in the City's contracts with other waste hauling services. (App. *infra*, A-5).

On March 11, 1993, the City's Utility Services/Land Use/Energy Development Committee reviewed their waste hauling contracts and recommended that the eight-year termination notices be given for all evergreen contracts. The committee's recommendation was not based on poor performance or other similar considerations, but was apparently motivated by a conclusion that shorter contracts would be better for the City. (App. *infra*, A-5).

On May 4, 1993 Newco filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Central District of California. Pursuant to 11 U.S.C. § 362, an automatic stay went into effect upon the filing of the bankruptcy petition. It is undisputed that the City was aware of Newco's filing of the bankruptcy petition. *See National Environmental Waste Corp. v. City of Riverside (In re National Environmental Waste Corp.)*, (9th Cir. 1997) (App., *infra*, A-8 n.3); *In re National Environmental Waste Corp.*, (Bankr. C.D. Cal. 1996) (App., *infra*, B-9 to B10). Nevertheless, even with that knowledge, on May 11, 1993, the City Council approved the committee's recommendation to terminate evergreen contracts, including the contract with Newco, in violation of the automatic stay. (App. *infra* A-5 to A-6).

On May 18, 1993, the City gave formal notice of the termination of the contract to Newco. Newco did not immediately protest this notice or inform the City that it was violating the automatic stay. The City, although aware of the existence of the bankruptcy action and the automatic stay, did

not seek any relief from the automatic stay or seek any other approval from the bankruptcy court at the time. Newco's Plan of Reorganization was confirmed by the bankruptcy court in 1994. (App. *infra* A-5 to A-6).

On April 10, 1995, Newco informed the City that it considered the notice of termination to be void as a violation of the automatic stay imposed by 11 U.S.C. § 362(a). The City then moved for an order determining that it's actions fell under the police and regulatory power exception to the automatic stay, 11 U.S.C. § 362(b)(4), or in the alternative, for an order retroactively annulling the automatic stay under 11 U.S.C. § 362(d)(1). The bankruptcy court denied the motion to determine that the police and regulatory power exception applied to the City's action, but granted the motion to annul the automatic stay with respect to City's termination of the contract. (App. *infra* B-13).

In an unpublished decision, the United States District Court for the Central District of California affirmed the order annulling the automatic stay and also dismissed the City's appeal from the portion of the order denying it's motion to determine that its actions fell within the police and regulatory power exception to the automatic stay. (App. *infra* E-1 to E-4).

Newco then appealed the district court's affirmance of the order annulling the automatic stay to the United States Court of Appeals for the Ninth Circuit ("Ninth Circuit"), under 28 U.S.C. § 158(d). The City also appealed the district court's order dismissing its appeal as moot. The Ninth Circuit approved the bankruptcy court's retroactive annulment of the automatic stay with respect to the City's termination of the contract. The Ninth Circuit also affirmed the district court's dismissal of the City's appeal as moot. The question presented to the Ninth Circuit, which it answered affirmatively, was

whether under the Bankruptcy Code, 11 U.S.C. § 362, a court may retroactively annul an automatic stay for cause where the creditor violated the stay while having actual knowledge of the pendency of the bankruptcy proceedings and the debtor did not act in bad faith or engage in any egregious conduct.

REASONS FOR GRANTING THE PETITION

A clear split of authority exists among the Courts of Appeals, as well as the bankruptcy courts, regarding the proper standard for determining when an automatic stay under the Bankruptcy Code, 11 U.S.C. § 362, should be retroactively annulled. In addition, the decision below to retroactively annul an automatic stay where the creditor had knowledge of the bankruptcy and the debtor engaged in no egregious conduct or bad faith violates the plain language and intent of Bankruptcy Code § 362(d)(1) by imposing a *de facto* duty upon debtors to act affirmatively to protect and police the operation of the automatic stay, which is not in keeping with the intent of the automatic stay provision.[1] In addition, the decision below is clearly erroneous and should be rectified under this Court's error-correcting authority.

As the Ninth Circuit itself acknowledged, a split exists among the circuit courts as to the proper test for determining whether or not a creditor's motion to annul the automatic stay should be granted for equitable reasons. Indeed, the Ninth Circuit decision in this case is the only decision to

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[1]Placing this burden on a bankruptcy debtor is directly contrary to an earlier Ninth Circuit decision. *Schwartz v. United States (In re Schwartz)*, 954 F.2d 569, 572 (9th Cir. 1992) ("The Bankruptcy Code does not burden the debtor with a duty to take additional steps to secure the benefit of the automatic stay.").

approve annulment where the creditor had actual knowledge of the automatic stay and where the debtor did not act in bad faith or engage in any egregious conduct. Conflicting decisions are proliferating rapidly in virtually all circuits, and the need for guidance from this Court is crucial.

A. The Automatic Stay is a Fundamental Protection Provided by the Bankruptcy Code

Section 362(d)(1) of the Bankruptcy Code provides in part that "on request of a party in interest and after notice and hearing, the court shall grant relief from the stay . . . such as by terminating, annulling, modifying, or conditioning such stay for cause . . ." 11 U.S.C. § 362(d)(1). The automatic stay is among the most basic of debtor protections under bankruptcy law. *See Midlantic Nat'l Bank v. New Jersey Dep't of Envtl. Protection*, 474 U.S. 494, 503 (1986). *See also* S. Rep. No. 95-989, at 54 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5840.

As the First Circuit described so colorfully in *Soares v. Brockton Credit Union (In re Soares)*, 107 F.3d 969 (1st Cir. 1997),

> "the dead tree gives no shelter." T.S. Eliot, The Waste Land, I, The Burial of the Dead (1922). Like a shade tree, the automatic stay which attends the initiation of bankruptcy proceedings, 11 U.S.C. § 362(a), must be nurtured if it is to retain its vitality.

Soares, 107 F.3d at 971. Courts must accordingly react rigorously to violations of the automatic stay. *See Kalb v. Feuerstein*, 308 U.S. 433, 438-39 (1940); *In re Smith Corsets Shops, Inc.*, 696 F.2d 971, 977 (1st Cir. 1982).

At issue in this matter is the request of a creditor for an annulment of the automatic stay -- that is, a request that the court retroactively approve an action that, at the time it was taken, violated the automatic stay. A request for annulment is significantly different from a request to lift the stay. A request to lift a stay works prospectively and authorizes later conduct that would otherwise violate the stay, but does not validate actions that have already taken place. *See Ellis v. Consolidated Diesel Elec. Corp.*, 894 F.2d 371, 373 (10th Cir. 1990); *see also Audio Data Corp. v. Monus*, 789 S.W.2d 281, 285 (Tex. App. – Dallas 1990, n.w.h.) (bankruptcy court order dismissing case showed intent to terminate, rather than annul, the stay; therefore, order did not have retroactive application and did not provide basis for state trial court to reaffirm default judgment entered against debtor while stay was in effect). A request for annulment, on the other hand, is a request for judicial approval of an unlawful act.

B. The Courts of Appeals are Split as to What Constitutes Sufficient Cause to Justify Annulment of the Stay

There exists a clear split of authority among the courts of appeals, as well as among the bankruptcy courts, as to the standard for determining whether or not cause exists to annul an automatic stay, a split that can only be healed by the invocation of this Court's authority.

1. The Ninth Circuit Decision

The Ninth Circuit, in its decision below, began its discussion of the issue of annulment by acknowledging that its standard for determining whether or not cause exists differs from the test used in other circuits.

> Many courts have focused on two factors in determining whether cause exists to grant relief from the stay: (1) whether the creditor was aware of the bankruptcy petition; and (2) whether the debtor engaged in unreasonable or inequitable conduct, or prejudice would result to the creditor. *See, e.g., Easley v. Pettibone Mich. Corp.*, 990 F.2d 905, 911 (6th Cir. 1993) (suggesting that the stay does not apply "where the debtor unreasonably withholds notice of the stay and the creditor would be prejudiced if the debtor is able to raise the stay as a defense, or where the debtor is attempting to use the stay unfairly as a shield to avoid an unfavorable result"); *In re Confidential Investigative Consultants, Inc.*, 178 B.R. 739, 752 (Bankr. N.D. Ill. 1995) ("Although there is no bright line rule, the general trend has been to evaluate two key factors: whether the creditor had notice of the bankruptcy, and how long the debtor delayed in asserting the automatic stay as a defense.").

Newco, (App., *infra*, A-7 to A-8). As will be discussed *infra*, other courts of appeals, as well as a number of bankruptcy courts, have used different and often conflicting tests in determining whether annulment should be granted.

The Ninth Circuit explicitly rejected the two-pronged test it cited. In response to Newco's assertion that the City's knowledge of the bankruptcy and its own innocence of egregious conduct should be dispositive, the court stated that

> we have never held these two factors to be dispositive; instead, we have engaged in a case by case analysis. *See Christensen v. Tucson*

> *Estates, inc. (In re Tucson Estates, Inc.)*, 912 F.2d 1162, 1166 (9th Cir. 1990) ("'Cause' has no clear definition and is determined on a case by case basis."). Thus, this court, similar to others, balances the equities in order to determine whether retroactive annulment is justified. *See, e.g. Albany Partners Ltd. v. Westbrook (In re Albany Partners, Ltd.)*, 749 F.2d 670, 675-76 (11th Cir. 1984) (weighing the facts to find that retroactive relief was reasonable); *In re Murray*, 193 B.R. 20, 22 (Bankr. E..D. Cal. 1996) ("Balancing the equities here," the court denied retroactive relief because the creditor "nonchalantly and continuously acted in violation of the stay"); *In re Siverling*, 179 B.R. 909, 912 (Bankr. E.D. Cal. 1995) ("equity directs the court to grant . . . retroactive relief from the stay").

Newco, (App., *infra*, A-8). In applying its "case by case" analysis, the Ninth Circuit found that the bankruptcy court "did not abuse it discretion in weighing the equities in favor of the City." *Newco*, (App., *infra*, A-8 to A-9), *citing Confidential Investigative Consultants*, 178 B.R. at 743. Had some form of the two-pronged analysis been applied to the instant case, the result would clearly have been different, as the City was aware of the pendency of the bankruptcy and Newco engaged in no egregious conduct and did not exhibit any bad faith in its actions.

2. Standards Used by Other Courts of Appeals

Other courts of appeals, clearly in an effort to afford greater deference to the protections of the automatic stay,

have used different, and usually stricter, standards in determining whether an annulment should be granted.

a. *The First Circuit Applies a Strict Standard Based Upon A Creditor's Lack of Notice or a Debtor's Bad Faith*

According to the United States Court of Appeals for the First Circuit ("First Circuit"), an automatic stay should not be "dismantled without good reason." *Soares v. Brockton Credit Union (In re Soares)*, 107 F.3d 969, 977 (1st Cir. 1997). "Only a strict standard will ensure the accomplishment of" the goals of the automatic stay. *Id.* While the First Circuit acknowledges that it is difficult to create a standard that can be mechanically applied, and that each case is unique, ostensibly similar to the conclusion of the Ninth Circuit, it gives examples that demonstrate what standards should be applied – e.g. a creditor's lack of notice or a debtor's bad faith – that demonstrate that retroactive relief must "rest on a set of facts that is both unusual and unusually compelling." *Soares*, 107 F.3d at 977, *citing Mataya v. Kissinger (In re Kissinger)*, 72 F.3d 107, 109 (9th Cir. 1995); *In re Pulley*, 196 B.R. 502, 504 (Bankr. W.D. Ark. 1996).

In reaching its decision, the *Soares* court focused on the creditor's failure to notify a state court about the stay despite the creditor's knowledge that the bankruptcy had been filed. The *Soares* court noted that the creditor had been represented by counsel and did not claim misapprehension of the effects of the bankruptcy filing. The court also discounted the debtor's failure to file any timely objections to the creditor's actions. *Soares*, 107 F.3d at 978. The court concluded by noting that while courts do possess some "limited discretion to grant retroactive relief from the automatic stay, instances in

which the exercise of that discretion is justified are likely to be few and far between." *Soares*, 107 F.3d at 977.

In an earlier case, *In re Smith Corsets Shops, Inc.*, 696 F.2d 971 (1st Cir. 1982), a creditor brought a trespass and ejectment action in state court against the debtor, not knowing that the debtor had filed for Chapter 11 reorganization. The First Circuit accepted the bankruptcy court's determination that section 362 did not make the creditor's actions illegal because the creditor acted in good faith in ignorance of the pendency of the bankruptcy petition and because the debtor's unreasonable behavior by "remain[ing] stealthily silent" contributed to the creditor's problem. *Smith Corsets*, 696 F.2d at 977.

The differences between the Ninth Circuit analysis and the standards articulated by the First Circuit present more than mere academic distinctions. Indeed, if the facts of the instant case had been analyzed under the *Soares* framework, annulment obviously would have been denied, as the City did have knowledge of the pendency of the bankruptcy. In addition, the *Soares* court would have given little if any weight to Newco's failure to object immediately to the termination of the contract.

b. *The Sixth Circuit Applies the Two-pronged Analysis Rejected by the Ninth Circuit.*

In *Easley v. Pettibone Michigan Corp.*, 990 F.2d 905 (6th Cir. 1993), the United States Court of Appeals for the Sixth Circuit ("Sixth Circuit"), addressing the issue of whether

or not actions taken in violation of a stay are void or voidable,[2] stated that "only where the debtor unreasonably withholds notice of the stay and the creditor would be prejudiced if the debtor is able to raise the stay as a defense" or where the debtor is attempting to make unfair use of the stay to avoid an unfavorable result, will the court tamper with the sanctity of the stay. *Easley*, 990 F.2d at 911.

The Sixth Circuit's two-pronged test, requiring creditor ignorance of the bankruptcy and some improper conduct on the part of the debtor, creates a much higher standard that must be met before the court will reduce the protections given by the stay. As the Ninth Circuit itself seemed to suggest, this two-pronged analysis used the by Sixth Circuit would have led to a far different result in the instant

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2 The courts of appeals also appear to be split on whether an action taken in violation of the automatic stay is void or merely voidable. A number of circuits have held that acts in violation of the automatic stay are void *ab initio*. *See, e.g. In re Siciliano*, 13 F.3d 748, 750-51 (3d Cir. 1994); *Matthews v. Rosene*, 739 F.2d 249, 251 (7th Cir. 1984); *Albany Partners Ltd. v. Westbrook (In re Albany Partners)*, 749 F.2d 670, 675 (11th Cir. 1987). Other circuits have concluded that such acts are only voidable. *See, e.g. Easley v. Pettibone Michigan Corp.*, 990 F.2d 905, 909-11 (6th Cir. 1993); *Sikes v. Global Marine, Inc.*, 881 F.3d 176, 178-79 (5th Cir. 1989). The "void" versus "voidable" may affect the request for an annulment to the extent that it determines which party has the burden on the annulment question. The Ninth Circuit in *Newco* appears to agree with most of the circuits that the action is void, yet seems to place the burden on the debtor to establish that the stay should not be annulled. *Newco*, (App., *infra*, A-7), *citing Schwartz v. United States* (*In re Schwartz*), 954 F.2d 569, 571-72 (9th Cir. 1992).

case. The City was well aware of the bankruptcy, which would itself halt any attempt to annul the stay under the Sixth Circuit standard. In addition, Newco did not withhold notice of the stay, Newco did not attempt to make any unfair use of the stay, and no actual evidence of prejudice was presented.

c. *The Seventh Circuit Requires Extraordinary Culpability on the Part of the Debtor to Justify Annulment of the Stay.*

In *Matthews v. Rosene*, 739 F.2d 249 (7th Cir. 1984), the United States Court of Appeals for the Seventh Circuit ("Seventh Circuit") determined that sufficient cause for annulment existed where enforcing the stay would seriously prejudice the creditor because of the debtor's extraordinary culpability where the debtor "unreasonably and inexcusably delayed asserting his claim against state court jurisdiction to the bankruptcy court." *Matthews*, 739 F.2d at 251.

While somewhat similar to the Ninth Circuit analysis, in that this standard does not require creditor ignorance of the pendency of the bankruptcy, the Seventh Circuit's test does impose an additional requirement on a party requesting annulment – that the moving party demonstrate some extraordinary culpability on the part of the debtor. In the instant case, the City made no such showing. There is no evidence in the record that Newco engaged in any improper conduct, and indeed, the bankruptcy court found to the contrary.

d. *The Tenth Circuit Requires the Creditor to be Honestly Ignorant of the Pendency of the Bankruptcy Proceedings.*

In *Franklin Savings Ass'n v. Office of Thrift Supervision*, 31 F.3d 1020 (10th Cir. 1994), the Director of the OTC had filed a bill of costs in district court following dismissal of an action brought against the Director by Franklin, which later filed for Chapter 11 relief. The district court denied the request for costs on the ground that it violated the automatic stay and refused to lift the stay nunc pro tunc. The United States Court of Appeals for the Tenth Circuit ("Tenth Circuit") affirmed the denial of the motion to annul the stay, stating that granting a request for annulment would be "rare and probably available only to claimants who were honestly ignorant of the bankruptcy stay." *Franklin*, 31 F.3d at 1023, *citing In re Pinetree, Ltd.*, 876 F.2d 34, 38 (5th Cir. 1989); *Albany Partners Ltd. v. Westbrook (In re Albany Partners, Ltd.)*, 749 F.2d 670, 675-76 (11th Cir. 1984).

In an earlier decision, *Calder v. Job (In re Calder)*, 907 F.2d 953 (10th Cir. 1990), the Tenth Circuit concluded that there should also be some culpability on the part of the debtor. In *Calder*, the Tenth Circuit addressed an alleged violation of the stay, noting that "courts will apply equitable considerations at least where the creditor was without actual knowledge of a bankruptcy petition and the bankrupt's unreasonable behavior contributed to the creditor's plight." *Calder*, 907 F.2d at 956, *citing In re Smith Corsets Shops, Inc.*, 696 F.2d 971, 976-77 (1st Cir. 1982).

These two decisions appear to set out a two-pronged analysis similar to that articulated by the Sixth Circuit – a requirement that the creditor be honestly ignorant of the pendency of the bankruptcy coupled with some improper or

unreasonable behavior on the part of the debtor. This standard also provides much more protection for the principles behind the automatic stay than that resulting under the Ninth Circuit's case-by-case analysis. Again, under this two-pronged test, the City's actual knowledge of the bankruptcy, coupled with a lack of any unreasonable behavior on the part of Newco, would have led to a denial of the request for annulment.

e. *The Eleventh Circuit Allows Annulment Where a Debtor has Acted in Bad Faith*

In its decision in *Albany Partners Limited v. Westbrook (In re Albany Partners, Ltd.)*, 749 F.2d 670 (11th Cir. 1984), the United States Court of Appeals for the Eleventh Circuit ("Eleventh Circuit") was presented with the situation where the creditor knew of the bankruptcy filing but went ahead with a foreclosure sale. The Eleventh Circuit affirmed the granting of the annulment anyway because it determined that debtor made a bad faith bankruptcy filing and the subject property had been previously adjudicated as not belonging to the debtor's estate. *Albany Partners*, 749 F.2d at 675-76.

The Eleventh Circuit's analysis also imposes an additional standard not used by the Ninth Circuit – some level of culpability on the part of the debtor. Under the reasoning set out in *Albany Partners*, Newco's lack of culpability should have protected it from a request to have the stay annulled.

f. *Various Bankruptcy Courts in Addressing the Issue Have Applied Varying Standards.*

Many bankruptcy courts have been confronted with the issue of when annulment is proper, and have applied varied standards to the question. The divisions among the bankruptcy courts mirror, and sometimes amplify, the split

among the courts of appeals. *See, e.g. In re The Elder-Beerman Stores Corp.*, 195 B.R. 1012, 1017 (Bankr. S.D. Ohio 1996) (bankruptcy court denied request for annulment , noting that factors to be considered are debtor's bad faith in filing the bankruptcy petition and moving party's knowledge of the bankruptcy at the time of its action); *In re Halas*, 194 B.R. 605, 614 (Bankr. N.D. Ill. 1996) (citations omitted) (court granted request for annulment where creditor was without actual knowledge of applicability of automatic stay and application of stay would unfairly prejudice creditor); *In re Pulley*, 196 B.R. 502, 504 (Bankr. W.D. Ark. 1996) (bankruptcy court granted motion for annulment upon showing that creditor was unaware of bankruptcy case and showing of prejudice or some element of bad faith on the part of the debtor). *See also Scrima v. John Devries Agency, Inc.*, 103 B.R. 128 (W.D. Mich. 1989) (district court reversed bankruptcy's courts granting of retroactive relief from automatic stay for postpetition cancellation of an insurance policy based upon the lack of any culpability or bad faith on the part of the debtor).

3. Intervention by This Court is Necessary to Resolve This Split of Authority

As demonstrated above, there exists a clear split of authority on the issue of annulment of the automatic stay. The Ninth Circuit decision is inconsistent with the rulings in other circuits, as well as with the rulings of numerous bankruptcy courts and its own prior decisions.[3] Had the facts of the instant case been subjected to one or more of the differing

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[3] *See e.g., Mataya v. Kissinger (In re Kissinger)*, 72 F.3d 107, 109 (9th Cir. 1995) (retroactive annulment to be "applied only in extreme circumstances."), *citing In re Shamblin*, 890 F.2d 123, 126 (9th Cir. 1989).

standards applied by the various cited courts, the ultimate decision would have been different, and would have resulted in a reversal of the bankruptcy court's granting the request for annulment. Guidance from this Court is needed to resolve these obviously conflicting authorities. If allowed to stand, the decision of the Ninth Circuit will wither, rather than nurture, the automatic stay.

C. The Ninth Circuit's Decision Violates the Clear Language and Intent of the Automatic Stay Provision of the Bankruptcy Code

The Ninth Circuit decision below violates the plain language of section 362 of the bankruptcy code and operates as a fundamental attack on the protections offered by the automatic stay. Indeed, the Ninth Circuit decision is the only case to affirm annulment where the creditor acted in knowing violation of the stay and where the debtor was not guilty of bad faith or egregious conduct. The Ninth Circuit decision, however, presents an even greater danger to the operation of the automatic stay.

In its "case-by-case" analysis of the "equities," the Ninth Circuit noted that

> the City is represented by counsel and, if it knew of the bankruptcy, it must have or should have known about the automatic stay. However, Newco is also represented by counsel and knew enough to warn the City about an unrelated act being a potential violation of the stay, yet it failed to object to the City's termination of the contract as such a violation.

Newco (App., *infra*, A-9)

In its "case by case" analysis, the court seems to read into section 362(a)(1) a requirement that a debtor represented by counsel warn the creditor about potential violations of the automatic stay. Nothing in the language of the statute imposes such a requirement. Indeed, imposing such a duty on debtors would lead to chaos, allowing creditors who knew of the stay to violate the stay with impunity and have their violations retroactively approved.

This decision is clearly not justified under the automatic stay provisions of the Bankruptcy Code. The automatic stay is designed to be just that – automatic, operating "without the necessity for judicial intervention." *Sunshine Dev., Inc. v. FDIC*, 33 F.3d 106, 113 (1st Cir. 1994). As the First Circuit noted in *Soares*, "if retroactive relief becomes commonplace, creditors – anticipating *post facto* validation – will be tempted to pursue claims against bankrupts heedless of the stay," forcing debtors to defend themselves for "fear that post-petition default judgments routinely may be resuscitated." *Soares*, 107 F.3d at 977. The First Circuit stated specifically that "Congress created the automatic stay to ward off scenarios of this sort." *Id.*

Indeed the Ninth Circuit itself recognized the potential dangers of such a requirement in one of its own earlier decisions. In *In re Shwartz*, 954 F.2d 569 (9th Cir. 1992), the Ninth Circuit, in addressing the "void" versus "voidable" issue discussed *supra*, noted the importance of enforcement of the stay.

> If violations of the stay are merely voidable, debtors must spend a considerable amount of time and money policing and litigating creditor actions. If violations are void, however, debtors

> are afforded better protection and can focus their attention on reorganization.

Schwartz, 954 F.2d at 571.

In addition, the Ninth Circuit's case-by-case analysis simply does not give sufficient deference to the automatic stay provision of the Bankruptcy Code. Other authorities have recognized the importance of safeguarding the protections provided by the automatic stay. Collier on Bankruptcy has specifically addressed the dangers arising from more frequent granting of retroactive annulment. "The breathing room provided by the stay would be limited if debtors feared regular retroactive validation." Collier on Bankruptcy, § 632.11[1] at 362-116 (citations omitted). If the monitoring and policing requirement implied in the Ninth Circuit decision is imposed, "debtors would be forced to defend all actions, even those stayed, because the stay might be retroactively annulled and a default by the debtor may become binding." *Id.* The potential dangers posed to the automatic stay clearly suggest that the Ninth Circuit's decision is unwarranted, given that "retroactive relief should be granted only in extraordinary circumstances, such as when a creditor acted without knowledge of the stay" or where the a motion to lift the stay would have been granted and the creditor actually changed its position in reliance on the validity of the action. *Id.*. The cavalier granting of retroactive relief, based on a failure of the debtor to warn of potential violations of the stay, is simply not acceptable under the clear language of the Bankruptcy Code. *See also* West's Hornbook on Bankruptcy (Practitioner's Edition) § 3-32, at 353-54 (citations omitted) (test for annulment is "decidedly two pronged").

The Ninth Circuit's imposition of a responsibility on debtors to police the operation of the

automatic stay is clearly inconsistent with the language and intent of the bankruptcy code. The decision is also inconsistent with the case law from other circuits, which all require at least a lack of knowledge on the part of the creditor or some deliberate, egregious conduct, on the part of the debtor. If the decision is allowed to stand, fundamental principles of the bankruptcy code will be jeopardized.

D. The Ninth Circuit's Decision is Clearly Erroneous and Should be Overturned Under This Court's Error-Correcting Authority

The Ninth Circuit decision is clearly out of line with other courts and erroneously approved annulment of the stay where a creditor knowingly violated the legal duties imposed by the stay. Even applying the case-by-case "equitable principles" analysis used by the court below, the decision is erroneous. There was no bad faith or egregious conduct by the debtor. Newco's actions did not mislead anyone. The City had actual knowledge of the bankruptcy, which is the legal equivalent of knowledge of the automatic stay. *In re Zartun*, 30 B.R. 543, 546 (Bankr. 9th Cir. 1983), *citing Fidelity Mortgage Investors Co. v. Camelia Builders, Inc.*, 550 F.2d 47 (2d Cir. 1976), *cert. denied*, 429 U.S. 1093 (1977). A fundamental principle of equity jurisprudence is that one who seeks equitable relief must come into court with clean hands. By definition, a party that has knowingly violated the law does not have clean hands.

The Ninth Circuit's efforts to balance the equities in favor of the City are simply not persuasive and are clearly erroneous. The Ninth Circuit's citation to the bankruptcy disclosure statement's recitation of cancellation is not controlling. The disclosure statement included nothing regarding the validity of the City's actions and merely

represented compliance by the debtor with 11 U.S.C. § 1125 requirements of disclosure. (App. *infra* H-4 to H-5). In addition, Newco's delay in challenging cancellation is not controlling, under the Ninth Circuit's own precedents. *See Schwartz v. United States* (*In re Schwartz*), 954 F.2d 569, 571-72 (9th Cir. 1992) (debtor waited more than three years to challenge action).

The Ninth Circuit also failed to rely upon actual evidence of prejudice to any party, a factor relied upon by nearly all the other courts to address this issue. The general discussion of potential prejudice contained in the opinion below is just that, a general discussion based on mere speculation. In reality, the only actual prejudice that might have existed is that which would have resulted from a court's proper refusal to protect the creditor from the consequences of its own illegal actions.

In sum, the Ninth Circuit rewarded a creditor for its knowing violation of the automatic stay, hardly the equitable result that should have obtained under the court's "case-by-case" balancing of the equities. In addition, the result below, as discussed *supra*, imposes a duty on debtors to immediately challenge a violation of the automatic stay, a duty not recognized by the bankruptcy code. The decision was clearly erroneous and should be corrected by this Court.

CONCLUSION

The questions presented in this petition are important questions of bankruptcy law with national implications. The marked split among the courts of appeals is in need of correction. The Ninth Circuit's imposition of a duty on debtors to police the operation of the automatic stay is inconsistent with the clear language and clear intent of the

bankruptcy code. In addition, the Ninth Circuit's decision was clear error and should be corrected. The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

In re:
NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation,
Debtor.

NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation,
Appellant,

v.

CITY OF RIVERSIDE, a political subdivision of the State of California,
Appellee.

No. 96-55825
D.C. No. CV-96-00299 LHM

In re:
NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation,
Debtor.

CITY OF RIVERSIDE, a political subdivision of the State of California,
Appellant,

v.

NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation,
Appellee.

No. 96-55852
D.C. No. CV-96-00300 LHM
OPINION

Appeals from the United States District Court
for the Central District of California
Linda H. McLaughlin, District Judge, Presiding

Argued and Submitted
October 8, 1997—Pasadena, California

Filed November 10, 1997

Before: Stephen Reinhardt and A. Wallace Tashima,
Circuit Judges, and Milton I. Shadur, District Judge.*

Opinion by Judge Tashima

SUMMARY

Bankruptcy/Automatic Stay

The court of appeals affirmed orders of the district court. The court held that a retroactive annulment of the automatic bankruptcy stay is supported by a represented Chapter 11 debtor's long delay in objecting to a substantial notice of a contract's termination relied on by the debtor in obtaining confirmance of its reorganization plan.

Appellant National Environmental Waste Corporation (Newco) and three other waste haulers had year-to-year "evergreen" contracts with appellee City of Riverside: the contracts renewed automatically, subject to the City's right to cancel without cause on eight years' notice.

On May 4, 1993, Newco filed a Chapter 11 bankruptcy petition. At a May 11 City Council meeting in which Newco

*The Honorable Milton I. Shadur, Senior United States District Judge for the Northern District of Illinois, sitting by designation.

and the other waste haulers participated, the City approved the earlier recommendation of its Utility Service Committee to terminate the contracts. When it obtained confirmation of its reorganization plan in 1994, Newco relied on the contract's cancellation. In April 1995, Newco notified the City that it considered the notice of termination to be a violation of the automatic stay.

The City moved for an order determining that the contract termination was within the exception to the automatic stay for actions taken pursuant to the police and regulatory powers of a government entity. Alternatively, the City asked for an order retroactively annulling the stay.

The bankruptcy court issued an order annulling the automatic stay with respect to the termination of the City's contract with Newco. The district court affirmed. Both sides appealed.

Newco asserted that the City's knowledge of the bankruptcy and its own innocence of egregious conduct were dispositive.

[1] The bankruptcy court has wide latitude in crafting relief from the automatic stay, including the power to grant retroactive relief. [2] Although there is no bright line rule, courts generally evaluate two factors: whether the creditor had notice of the bankruptcy, and how long the debtor delayed in asserting the automatic stay. [3] Courts engage in a case-by-case analysis, and balance the equities to determine whether retroactive annulment is justified.

[4] The bankruptcy court did not abuse its discretion in weighing the equities in favor of the City. The City was represented by counsel and, if it knew about the bankruptcy, it must or should have known about the automatic stay. However, Newco was also represented and knew enough to warn the City that any attempt to recover excess dump fees would

be a violation of the stay. Newco even confirmed its reorganization plan in reliance on the termination of the contract.

[5] Other factors the court considered included the length of the required notice period in the contract; prejudice to the City by giving Newco exclusive rights in serving the City for three additional years; Newco's "reinforcement" of the perception that termination was valid by failing to challenge it either at the City Council meeting or in its reorganization plan; possible prejudice to other parties who confirmed the plan in reliance on the eight-year notice; lack of prejudice to Newco if the stay were annulled; and the court's reliance on the fact that it would have granted the relief had the City applied beforehand.

[6] The district court's affirming of the bankruptcy court's grant of retroactive relief from the automatic stay rendered moot the question of whether the termination was an exercise of the City's police and regulatory power.

COUNSEL

William M. Burd, Burd & Naylor, Santa Ana, California, for the appellant in No. 96-55825 and the appellee in No. 96-55852.

J. Scott Williams, Rus, Miliband, Williams & Smith, Irvine, California, for the appellee in No. 96-55825 and the appellant in No. 96-55852.

OPINION

TASHIMA, Circuit Judge:

Debtor National Environmental Waste Corporation ("Newco") appeals the district court's affirmance of the bank-

ruptcy court's retroactive annulment of the automatic stay. Because of the unusual circumstances of this case, we conclude that the bankruptcy court did not abuse its discretion in granting retroactive relief from the stay.

I. BACKGROUND

Newco has provided waste hauling services in a portion of the City of Riverside ("City") since 1972. Since 1991, the City has been divided into five areas for purposes of solid waste handling services, retaining four different solid waste enterprises to service those areas. In 1991, Newco entered into a contract with the City to provide waste handling services. It was an "evergreen" contract, meaning it was automatically renewed from year to year, subject to the City's right to cancel without cause upon eight years' notice. The City's contracts with the other three solid waste enterprises were also evergreen contracts.

On March 11, 1993, the City's Utility Services/Land Use/Energy Development Committee, at the request of the Riverside City Council, reviewed the four evergreen contracts. The Committee concluded that the eight-year notice requirement did not allow the City to provide best for its constituents. It thus recommended that the eight-year termination notices be given. The Committee stressed that its recommendation was not due to poor performance by the waste haulers, but was based on its conclusion "that it is simply good public policy to review the contracts periodically to ensure competition, innovation and the best possible service to the City's businesses and residents."

On May 4, 1993, Newco filed a Chapter 11 petition in bankruptcy. On May 11, 1993, at a meeting in which representatives of Newco and the other waste haulers participated, the City Council approved the Committee's recommendation to terminate the evergreen contracts. On May 18, 1993, the City gave notice of termination to all four solid waste enter-

prises serving the City, including Newco. Newco's Plan of Reorganization was confirmed in 1994.[1] On April 10, 1995, Newco informed the City that it considered the notice of termination to be void as a violation of the automatic stay imposed by 11 U.S.C. § 362(a).

The City moved for an order determining that its actions fell under 11 U.S.C. § 362(b)(4), the police and regulatory power exception to the automatic stay or, in the alternative, for an order retroactively annulling the automatic stay. The bankruptcy court denied the motion to determine that the police and regulatory power exception applied to the City's actions, but granted the motion to annul the automatic stay with respect to the City's termination of the contract. *In re National Envtl. Waste Corp.*, 191 B.R. 832 (Bankr. C.D. Cal. 1996). The district court affirmed the order annulling the automatic stay and dismissed the City's appeal from the portion of the order denying its motion to determine that its actions fell within the police and regulatory power exception to the automatic stay.

II. JURISDICTION AND STANDARDS OF REVIEW

In No. 96-55825, Newco appeals the district court's affirmance of the order annulling the automatic stay. In No. 96-55852, the City appeals the district court's order dismissing its appeal as moot. Orders granting or denying relief from the automatic stay are deemed to be final orders. *Bender Corp. v. Conejo Enters., Inc. (In re Conejo Enters., Inc.)*, 96 F.3d 346, 351 (9th Cir. 1996). As these appeals are from such final orders, we have jurisdiction under 28 U.S.C. § 158(d). The decision of the bankruptcy court is reviewed de novo, without deference to the district court's determinations. *Robertson v. Peters (In re Weisman)*, 5 F.3d 417, 419 (9th Cir. 1993). A decision retroactively to lift the automatic stay is reviewed for

[1] As discussed below, the Plan assumed that Newco's contract with the City would terminate in accordance with the notice given in 1993.

an abuse of discretion. *Mataya v. Kissinger (in re Kissinger)*, 72 F.3d 107, 108 (9th Cir. 1995). Finally, because it presents a question of law, we review the district court's mootness decision de novo. *Arnold & Baker Farm v. United States (In re Arnold & Baker Farm)*, 85 F.3d 1415, 1419 (9th Cir. 1996), *cert. denied*, 117 S.Ct. 681 (1997).

III. DISCUSSION

[1] Pursuant to 11 U.S.C. § 362, a petition in bankruptcy operates as a stay against acts that may affect property of the bankruptcy estate. The automatic stay is designed to "protect debtors from all collection efforts while they attempt to regain their financial footing." *Schwartz v. United States (In re Schwartz)*, 954 F.2d 569, 571 (9th Cir. 1992). It is also designed to protect creditors from the "race of diligence," in which those who acted first would receive payment "in preference to and to the detriment of other creditors." H.R. Rep. No. 95-595, at 340 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6297. Actions taken in violation of the stay are void. *Schwartz*, 954 F.2d at 571-72. However, section 362(d) "gives the bankruptcy court wide latitude in crafting relief from the automatic stay, including the power to grant retroactive relief from the stay." *Id.* at 572.[2]

[2] Many courts have focused on two factors in determining whether cause exists to grant relief from the stay: (1) whether the creditor was aware of the bankruptcy petition; and (2) whether the debtor engaged in unreasonable or inequitable conduct, or prejudice would result to the creditor. *See, e.g., Easley v. Pettibone Mich. Corp.*, 990 F.2d 905, 911 (6th Cir. 1993) (suggesting that the stay does not apply "where the debtor unreasonably withholds notice of the stay and the cred-

[2]Section 362(d)(1) provides in relevant part, "On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay . . . such as by terminating, annulling, modifying, or conditioning such stay—for cause . . . ."

itor would be prejudiced if the debtor is able to raise the stay as a defense, or where the debtor is attempting to use the stay unfairly as a shield to avoid an unfavorable result"); *In re Confidential Investigative Consultants, Inc.*, 178 B.R. 739, 752 (Bankr. N.D. Ill. 1995) ("Although there is no bright line rule, the general trend has been to evaluate two key factors: whether the creditor had notice of the bankruptcy, and how long the debtor delayed in asserting the automatic stay as a defense.").

[3] Newco asserts that the City's knowledge of the bankruptcy and its own innocence of egregious conduct should be dispositive in this case.[3] However, we have never held these two factors to be dispositive; instead, we have engaged in a case by case analysis. *See Christensen v. Tucson Estates, Inc. (In re Tucson Estates, Inc.)*, 912 F.2d 1162, 1166 (9th Cir. 1990) (" 'Cause' has no clear definition and is determined on a case by case basis."). Thus, this court, similar to others, balances the equities in order to determine whether retroactive annulment is justified. *See, e.g., Albany Partners, Ltd. v. Westbrook (In re Albany Partners, Ltd.)*, 749 F.2d 670, 675-76 (11th Cir. 1984) (weighing the facts to find that retroactive relief was reasonable); *In re Murray*, 193 B.R. 20, 22 (Bankr. E.D. Cal. 1996) ("Balancing the equities here," the court denied retroactive relief because the creditor "nonchalantly and continuously acted in violation of the stay"); *In re Siverling*, 179 B.R. 909, 912 (Bankr. E.D. Cal. 1995) ("equity directs the court to grant . . . retroactive relief from stay").

[4] Although the conduct of neither party was exemplary, "either . . . not recogniz[ing] the problem or recogniz[ing] it and proceed[ing] . . . without doing anything about it," we find that the bankruptcy court did not abuse its discretion in

[3]Although it is not entirely clear from the record, the bankruptcy court found that the City had actual knowledge of the bankruptcy. We defer to this finding of fact, as it is not clearly erroneous. *See Weisman*, 5 F.3d at 419.

weighing the equities in favor of the City. *In re Confidential Investigative Consultants, Inc.*, 178 B.R. at 743. The City is represented by counsel and, if it knew of the bankruptcy, it must have or should have known about the automatic stay. However, Newco is also represented by counsel and knew enough to warn the City about an unrelated act being a potential violation of the stay,[4] yet it failed to object to the City's termination of the contract as such a violation.[5] Newco even confirmed its reorganization plan in reliance on the termination of the contract, raising the issue only after confirmation. Further, the City terminated its evergreen contracts with all of its waste haulers, not just Newco, because of the eight-year notice requirement. These unusual circumstances support the bankruptcy court's decision.

[5] Other factors the court considered include the length of the required notice period in the contract (eight years); prejudice to the City by giving Newco exclusive rights in serving the City for three additional years; Newco's "reinforcement" of the perception that the termination was valid by failing to challenge it either at the May 11, 1993, City Council meeting or in its reorganization plan;[6] possible prejudice to other parties who confirmed the plan in reliance on the eight-year termination notice; and lack of prejudice to Newco if the stay were annulled. The court's reliance on the fact that it would

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[4]On May 28, 1993, Newco informed the City that any attempt to recover excess dump fees would be a violation of the automatic stay.

[5]The debtor's awareness of his or her rights has been considered by one court in the analysis of whether to annul the stay. In *Scrima v. John DeVries Agency, Inc.*, 103 B.R. 128 (W.D. Mich. 1989), on which Newco relies, the fact that the debtor was unaware of his rights under the automatic stay was important to the court's conclusion. *Id.* at 134. In contrast, Newco has been represented by counsel throughout.

[6]Newco analogizes its conduct to the debtors' three-year delay in *Schwartz*. However, in *Schwartz*, the sole issue was whether such violations of the stay are void or voidable. 954 F.2d at 570-71. We stated that a court has power to ratify retroactively a violation of the stay, but did not address the issue of retroactive annulment in that case. *Id.* at 573.

have granted the relief had the City applied beforehand is also a valid factor on which to rely in granting retroactive relief. *See Kissinger*, 72 F.3d at 109.

We conclude, in light of all of the factors involved, that the bankruptcy court did not abuse its discretion in granting the City retroactive annulment of the automatic stay.

[6] In its own appeal, the City addresses only the merits and not the district court's dismissal of its appeal as moot. However, its motion in the bankruptcy court was in the alternative, suggesting that if the City prevailed on either part of its motion, it would obtain all of the relief that was necessary. We agree with the district court that affirming the bankruptcy court's grant to the City of retroactive relief from the automatic stay for purposes of the City's termination of the evergreen contract has rendered moot the question presented in the City's appeal of whether the termination was an exercise of the City's police and regulatory power.

IV. CONCLUSION

In No. 96-55825, the order of the district court affirming the bankruptcy court is **AFFIRMED.** In No. 96-55852, the order of the district court dismissing the City's appeal as moot is **AFFIRMED**. Because the latter appeal was a "protective" appeal, the City shall recover its costs on both appeals.

APPENDIX B

Filed January 25, 1996

Entered January 31, 1996

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In re	)	Chapter 11
	)	
NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California corporation aka NEWCO, aka NEWCO WASTE, aka NEWCO RECYCLING	)	Case No. SA 93-14825 JW
	)	**MEMORANDUM OF DECISION**
	)	Date: September 27, 1995
Reorganized Debtor.	)	Time: 9:15 a.m.
		Ctrm: 604

The City of Riverside ("Riverside" or the "City") filed a motion for an order determining that the police and regulatory power exception to the automatic stay applies to the City's review and termination of its solid waste contracts. Debtor National Environmental Waste Corporation ("Newco") opposed the motion on the ground that the City's action was void and not subject to any exceptions to the automatic stay in the Bankruptcy Code. The issues before the Court are (1) whether the actions of the City qualify under the automatic stay exception in Bankruptcy Code § 362 (b); and (2) whether the automatic stay can be annulled in this case with respect to the City's termination of its contract with Newco.

I. Statement of Facts

Newco has handled waste hauling services in the City of Riverside since approximately 1972. In 1991, the City retained four separate solid waste enterprises to service exclusively its five separate service areas. The agreements between Riverside and the waste hauling enterprises were known as "Evergreen" contracts, because they ran perpetually until the city provided notice of termination. On January 18, 1991, Newco entered into a contract with Riverside to provide refuse hauling services within the City. The contract was for a term of eight years and automatically renewed itself annually for another year subject to Riverside's right to provide eight years' notice of termination.

On March 11, 1993, Riverside's Utility Services/Land Use/Energy Development Committee, at the request of the Riverside City Council, reviewed the Evergreen contracts between the City and the various solid waste enterprises. The Committee determined that the Evergreen contracts did not allow the City to provide for the health and welfare of its constituents in the best possible way due to the eight year notice provisions.

On May 4, 1993, Newco filed a voluntary petition under Chapter 11 of the Bankruptcy Code, for reasons unrelated to the City's actions.

On May 11, 1993, the Riverside City Council, acting on a recommendation from the Committee, voted to terminate the Evergreen contracts, including the agreement with Newco. On May 18, 1993, Riverside provided notice of the termination to all the solid waste enterprises providing services to the City, including Newco.

On June 22, 1994, Newco confirmed its Chapter 11 Plan of Reorganization. On April 10, 1995, Newco advised Riverside that it considered the notice of termination to be void as having been issued in violation of 11 U.S.C. § 362(a).

On August 28, 1995, Riverside filed a motion for an order determining that the police and regulatory power exception to the automatic stay applies to the notice of termination sent by the City or, in the alternative, for an order annulling the automatic stay.

II. Discussion

Riverside makes two arguments in its motion: (1) the automatic stay provided by Section 362(b) (4) excepts the action of the City Council; and (2) even if Section 362 (b) (4) does not except Riverside's actions, the Court should grant an order annulling the automatic stay with respect to Riverside's termination of Newco's contract. While the Section 362(b) (4) exception does not apply to Riverside's termination of Newco's contract, the Court holds that, due to the unique facts presented in this case, equity requires that the Court annul the automatic stay with respect to the City's termination of Newco's contract.

A. The Police and Regulatory Power Exception to the Automatic Stay Found in Bankruptcy Code Section 362 (b) (4) Does Not Apply to Riverside's Termination of Newco's Contract.

Pursuant to Ninth Circuit law, Newco's contract with the City constitutes property of the estate. Thus, unless an exception applies, any act to obtain possession or control over the contract is stayed pursuant to Bankruptcy Code Section 362(a)(3):

> (a) Except as provided in subsection (b) of this, a petition filed . . . operates as stay, applicable to all entities, of – . . .
>
> (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

It is well established in the Ninth Circuit that the contract rights of a debtor are property of the estate pursuant to Bankruptcy Code Section 541. For example, insurance contracts fall within the statutory definition of property under Section 541, and the right to cancel an insurance policy is stayed under Section 362(a)(3). *The Minoco Group of Companies, Ltd. v. First State Underwriters Agency of New England Reinsurance Corporation (In re The Minoco Group of Companies, Ltd.)*, 799 F.2d 517, 519 (9th Cir. 1986). In *Computer Communications, Inc. v. Codex Corporation (In re Computer Communications, Inc.)*, 824 F.2d 725, 728 (9th Cir. 1987), the Ninth Circuit stated:

> 11 U.S.C. § 362 provides that the filing of a bankruptcy petition automatically stays "any act to obtain possession of property of the estate . . . ."
>
> 11 U.S.C. § 362(a)(3). The courts below held that the automatic stay prohibited Codex from unilaterally terminating the Agreement. We agree. Even if Codex had a valid reason for terminating the Agreement, it still was required to petition the court for relief from the automatic stay under § 362(d).

In *Carroll v. Tri-Growth Centre City, Ltd. (In re Carroll)*, 903 F.2d 1266, 1271 (9th Cir. 1990), the Ninth Circuit reiterated that an executory contract that is property of the estate can only be terminated after a grant of relief from the stay. Thus, under Ninth circuit law, the contract between Newco and Riverside is property of the estate. Accordingly, the automatic stay of Section 362(a) protects Newco's contract rights from unilateral termination, unless some exception in Section 362(b) applies.

Riverside apparently concedes that Newco's contract rights are property of the estate. However, the City contends that the actions taken by the Council are excepted from the automatic stay by Section 362(b)(4). The subsection states:

> (b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a) (3) of the Securities Investor Protection Act of 1970, does not operate as a stay--...
>
> (4) *under subsection (a) (1)* of this section, of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power; (emphasis added).

On its face, this exception to the automatic stay only applies to the stay under subsection (a) (1) of Section 362, which provides that a bankruptcy filing operates as a stay as to:

> (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

However, the actions of the Council constitute an act to obtain possession of property of the estate and thus trigger the automatic stay provision in Section 362(a)(3).

Under the Ninth Circuit's reading of Section 362(b) (4), the City's attempt to exercise control over Newco's contract is a violation of the automatic stay. In *Hillis Motors, Inc. v. Hawaii Auto Dealers Association*, 997 F.2d 581 (9th Cir. 1993), the defendant argued that the actions of the Hawaii Department of Commerce and Consumer Affairs in purportedly dissolving a corporate debtor while the automatic stay was in effect, based on the debtor's failure to file annual exhibits and accompanying filing fees, were exempt from the automatic stay as an exercise of police or regulatory powers.

In holding the actions of the state to be void *ab initio*, the Ninth Circuit stated,

> Where through an action an individual or entity would exercise control over property of the estate, that party must obtain advance relief from the automatic stay from the bankruptcy court. [*Carroll*, 903 F.2d at 1270-71]. This rule applies with equal force to acts by governmental agencies.

Id. at 586.

The legislative history clearly indicates the scope of Section 362(b)(4):

> [Subsection (b) (4)] excepts commencement or continuation of actions and proceedings by governmental units to enforce police or regulatory powers. Thus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such law, the action or proceeding is not stayed under the automatic stay.

H.R. Rep. No. 595, 95th Cong., 1st Sess. 343 (1977); S. Rep. No. 989, 95th Cong, 2d Sess. 52 (1978).

> [Subsection (b)(4)] is intended to be given a narrow construction in order to permit governmental units to pursue actions to protect the public health and safety and not to apply actions by a governmental unit to protect a pecuniary interest in property of the debtor or property of the estate.

124 Cong. Rec. H11092 (daily ed. Sept. 28, 1978); S17409 (daily ed. Oct. 6, 1978); remarks of Rep. Edwards and Sen. DeConcini.

In other words, Congress designed Section 362 (b) (4) to allow governments to act pursuant to their traditional regulatory and police powers to protect public health and safety. Not all actions of governments are actions pursuant to such powers. Many governmental actions are conducted in the government's capacity as a commercial actor. In such instances, the governmental unit should be held to the same standards of action as any non-governmental unit.

The City relies on a recent U.S. Supreme Court case, *Citizens Bank of Maryland v. Strumpf*, for the proposition that Section 362 (a) (3) should not be applied to restrict governmental actions such as the City's termination of Newco's contract. *Citizens Bank of Maryland v. Strumpf*, __ U.S. __, 95 D.J. DAR 14562 (November 1, 1995). In *Strumpf*, the U.S. Supreme Court held that a bank's post-petition administrative hold on a debtor's account did not violate the automatic stay. In support of its argument that the administrative hold did not constitute a setoff, Citizens Bank of Maryland argued that Section 542(b) specifically recognizes a creditor's right to setoff in turning over property of the estate and that Section 553(a) preserves a creditor's non-bankruptcy right of setoff. In response, the debtor argued that the bank's administrative hold violated Section 362(a) (3), which prohibits any act to obtain possession of or exercise control over property of the estate. In rejecting the debtor's argument, the U.S. Supreme Court stated that it will not give Section 362 (a) (3) an interpretation that would proscribe what Sections 542 (b) and 553 (a) were plainly intended to permit. *Strumpf*, __ U.S. at __, 95 D.J. DAR at 14563.

Strumpf, however, is not directly on point. The U.S. Supreme Court found that the bank's administrative hold did not constitute an exercise of control or dominion over property of the estate; it was merely a refusal to perform its promise. Thus, the U.S. Supreme Court ruling rested not on a limitation of the scope of Section 362 (a) (3) , but on its

finding that the action at issue did not deprive the estate of property.

In this case, since Ninth Circuit law holds that contract rights constitute property of the estate, the City's unilateral termination of Newco's contract is clearly an action exercising control over property of the estate.

The City makes much of the fact that it decided to terminate all the Evergreen contracts to improve its negotiating position as somehow demonstrating that termination of the contract therefore falls within the police or regulatory power exception. However, the City's argument only demonstrates that its actions were commercial in nature and were not intended by Congress to fall within the police or regulatory power exception. The Third Circuit has explained the policy behind this exception as follows:

> Government agencies are only excepted from the reach of the automatic stay when proceeding "to enforce such governmental unit's police or regulatory power." 11 U.S.C. Section 362(b). Congress intended this exception to apply where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violations of such law . . . Neither the language of section 362(b) nor its legislative history indicates that this exception was intended to permit government agencies to enforce *contractual* rights against a debtor without first seeking relief from the automatic stay.

In re University Medical Center, 973 F.2d 1065, 1074-1075 (3d. Cir. 1992) (emphasis in the original) (footnotes and citations omitted).

Here, the City clearly exercised its contractual rights in violation of Section 362 (a) (3). Thus, the police or regulatory

power exception of Section 362(b) (4) does not excuse the City's actions.

In the Ninth Circuit, barring a retroactive annulment of the automatic stay, actions taken in violation of the automatic stay are void, not voidable. *Schwartz v. United States of America (In re Schwartz)*, 954 F. 2d 569 (9th Cir. 1992); *Hillis Motors*, 997 F.2d at 586. Thus, if the stay were to remain in force, the City's actions in violation of the automatic stay would be void.

B. The City Is Entitled to an Annulment of the Automatic Stay With Respect to the City Council's Termination of Its Contract With Newco.

Although actions taken in violation of the automatic stay are generally void, Section 362(d) (1) provides that a creditor affected by the imposition of the automatic stay may petition the Court for annulment of the stay and shall be entitled to such relief for cause. Annulment may be granted so as to retroactively validate actions taken post-petition. *Schwartz*, 954 F.2d at 569. Pursuant to Section 362(g) (2), the debtor has the burden of proof to demonstrate that "cause" does not exist to annul the stay under Section 362 (d) (1). 11 U.S.C. § 362(g)(2).

The City claims that Newco is estopped from challenging the City's termination of its contract under the doctrine of laches. While the cases that the City cites are largely inapposite to the instant case, the Court finds that equitable considerations justify annulment of the automatic stay with respect to the City's termination of the Newco contract.

The City cites two cases in support of its request for annulment of the automatic stay: *Job v. Calder (In re Calder)*, 907 F.2d 953 (l0th Cir. 1990) and *Matthews v. Rosene*, 739 F.2d 249 (7th Cir. 1984). These cases involved egregious conduct by the debtor, particularly in concealing the commencement of the bankruptcy proceeding. In this case, Newco's conduct did not rise to an egregious level, and the

City had actual knowledge of Newco's bankruptcy proceeding. Thus, these decisions are not controlling.

Here, we have a unique situation with facts that radically differ from previous cases, and the holdings in *Calder* and *Matthews* would produce an inequitable result if applied to the instant case. Most significantly, this case concerns a contract with an *eight-year notice of termination clause*. Furthermore, all parties involved in this case have acted throughout these proceedings on the assumption and belief that the City validly terminated Newco's contract in 1993.

Due to the length of the notice period (8 years), an order denying the City's motion for annulment would greatly prejudice Riverside by allowing Newco to have exclusive rights in providing a vital civil service for almost three additional years. If the City is held to have violated the automatic stay with its termination of the Newco contract, then the contract expires eight years after the City sends Newco a new notice of termination. If the City's termination of the Newco contract is valid, then the contract expires eight years from the notice, i.e., the year 2001.

While Newco did not engage in egregious conduct or "stealth silence," its actions nevertheless reinforced the perception that Newco's contract would indeed terminate eight years after the City's valid termination in 1993. Newco's representatives attended the City Council meeting at which the Evergreen contracts were discussed. The City notified Newco of its termination of the Newco contract on May 18, 1993; yet, Newco did not challenge the validity of the City's actions until April 10, 1995. Newco specifically acknowledged that the City had legally terminated its contract with Newco in pleadings filed in support of the plan confirmation:

> Much has been made of *the fact that Debtor's contract with the City will expire in May, 2001*. What this really means is that Debtor will have no

> competition in the City for approximately eight years of the Plan.

Declaration of Christy B. Reehl, filed by Newco, April 27, 1994. Newco disclosed but failed to challenge the validity of the City's review and termination in its Second Amended Joint Disclosure Statement To Accompany Debtors' First Amended Joint Plan Of Reorganization, filed on March 2, 1994, and approved by Order of this Court entered on March 8, 1995, wherein Newco stated that:

> On May 11, 1993, the City Council of the City of Riverside approved a recommendation to provide the required eight-year notice to the private refuse haulers (including Newco) to terminate their contracts. In a letter dated May 18, 1993, Newco received written notice from the City's Public Works Director that its contract with the City will expire on May 11, 2001.

Lastly, and most significantly, Newco confirmed its plan of reorganization by Order entered June 22, 1995, based on the assumption that the City had terminated Newco's contract and that the contract would expire in the year 2001.

While Newco was under no legal duty to inform the City that its termination of the Newco contract was a violation of the automatic stay, all parties to this process worked to confirm Newco's plan under the assumption that the contract would expire in 2001, and not 2004. Given the eight-year notice of termination provision in the contract, the City, and possibly other parties, would be prejudiced by Newco's assertion, made twenty-three months after the City's action, that the termination was a violation of the automatic stay and, hence, was void.

On the other hand, Newco will not be prejudiced by an annulment of the automatic stay that validates the City's termination of the contract. Newco had assumed all along that the contract would expire in 2001, pursuant to the City's

valid termination in 1993. Moreover, had the City applied to the Court for relief from the automatic stay to terminate the Newco contract, the Court would have routinely granted the motion. It would be inequitable to allow Newco to claim a violation of the automatic stay by the City nearly two years earlier and after the confirmation of its plan of reorganization based on a valid termination of the contract.

C. The City Is Not Entitled to an Award of Attorneys' Fees

The City requests an award of attorneys' fees pursuant to Paragraph 4 of the contract between it and Newco, which provides that:

> In the event of any litigation arising out of a breach of this contract, the prevailing party shall be entitled to an award of court costs including reasonable attorney's fees in connection with such litigation, in addition to all other relief to which such party shall be entitled.

However, this proceeding is a motion for annulment of the automatic stay, not "litigation arising out of a breach of this contract."

In *Johnson v. Righetti (In re Johnson)*, 756 F.2d 738 (9th Cir. 1985), the Ninth Circuit affirmed a district court decision denying a debtor's request for attorneys' fees incurred in defending a motion for relief from stay. In so doing, the Ninth Circuit stated,

> A request for relief from the automatic stay pursuant to 11 U.S.C. § 362(d) is not an "action on a contract" to which state substantive law would be applied but an action on a federal statute to be decided according to federal law.

Id. at 741-42. In light of the Ninth Circuit's holding in *Johnson*, and since there exists no statute that permits

recovery for attorneys' fees under these circumstances, the City is not entitled to recover attorneys' fees.

III. CONCLUSION

The automatic stay provisions of Section 362(a)(3) protected Newco's rights under the contract with the City. While Section 362(b)(4) provides for a police and regulatory power exception to the automatic stay imposed by Section 362(a)(1), there is no such exception to the automatic stay imposed by Section 362(a)(3). Thus, the City's motion for an order determining that the police or regulatory power exception to the automatic stay applies to the City Council's termination of the City's contract with Newco is denied.

Nevertheless, the City is entitled to annulment of the automatic stay regarding the City's termination of Newco's contract, due to the extenuating facts of this case. Thus, the City's motion for an order annulling the automatic stay is granted.

The City's request for attorneys' fees is denied.

This memorandum of decision contains this Court's findings of fact and conclusions of law. Counsel for Riverside shall lodge and serve a proposed order consistent with this memorandum of decision.

Dated: January 25, 1996

JOHN J. WILSON
UNITED STATES
BANKRUPTCY JUDGE

William B. Burd & Karen Sue Naylor for National Environmental Waste Corporation, Debtor.

J. Scott Williams, D. Edward Hays, Stan T. Yamamoto, Carolyn Confer for City of Riverside, Movant.

In re	Chapter 11
NATIONAL ENVIRONMENTAL WASTE CORPORATION	**CASE NO. SA93-14825JW**

NOTICE OF ENTRY OF JUDGMENT OR ORDER AND CERTIFICATE OF MAILING

TO ALL PARTIES IN INTEREST ON THE ATTACHED SERVICE LIST:

1. *You are hereby notified, pursuant to Local Bankruptcy Rule (116)(1)(a)(iv), that a judgment or order entitled (specify):*

MEMORANDUM OF DECISION JANUARY 31, 1996.

2. *I hereby certify that I mailed a copy of this notice and a true copy of the order or judgment to the persons and entities on the attached service list on (specify date):*

Dated: JANUARY 31, 1996

Jon D. Ceretto
Clerk of the
Bankruptcy Court

By: /s/ Jon D. Ceretto
Deputy Clerk

SERVICE LIST

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APPENDIX C

Filed: February 7, 1996

Entered: February 9, 1996

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Attorneys for the CITY OF RIVERSIDE,
a political subdivision of the
State of California

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In re:	) Bankruptcy No.
NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California corporation aka NEWCO, aka NEWCO WASTE, aka NEWCO RECYCLING,	) SA93-14825 JW)) PARTIALLY) CONSOLIDATED WITH) *In re International Rubbish*) *Service, Inc.*) Bankruptcy No.) SA 93-14824
Reorganized Debtor.	)
THE CITY OF RIVERSIDE,	) Chapter 11

a political subdivision of the State of California, Movant vs. NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California corporation aka NEWCO, aka NEWCO WASTE, aka NEWCO RECYCLING, Respondent.	ORDER (1) GRANTING MOTION TO ANNUL AUTOMATIC STAY FOR CAUSE AND (2) DENYING MOTION FOR ORDER DETERMINING POLICE AND REGULATORY POWER EXCEPTION TO AUTOMATIC STAY APPLICABLE TO ACTIONS TAKEN BY THE CITY OF RIVERSIDE RE SOLID WASTE COLLECTION Date: September 27, 1995 Time: 9:30 a.m. Ctrm: 604

The Motion For Order Determining Police And Regulatory Power Exception To Automatic Stay Applicable To Actions Taken By The City Of Riverside Re Solid Waste Collection Or, In The Alternative, For Order Annulling Automatic Stay For Cause ("Motion") filed by the City of Riverside came on for hearing on September 27, 1995 at 9:15 a.m. in Courtroom 604 of the above-entitled Court. The City of Riverside appeared by and through its attorneys of record, RUS, MILIBAND, WILLIAMS & SMITH, a Professional Corporation, by J. SCOTT WILLIAMS. The Debtor appeared by and through its counsel of record, the LAW OFFICES OF WILLIAM M. BURD, by WILLIAM M. BURD. No other appearances were made.

Upon due consideration of all papers and pleadings on file herein and the argument of counsel and the Court having stated its findings of fact and conclusions of law in its written Memorandum of Decision filed on January 25, 1996, and good cause appearing therefor,

IT IS HEREBY ORDERED that the Motion is granted in part and denied in part.

IT IS FURTHER ORDERED that, as to the City of Riverside, the automatic stay in this case is annulled to and including May 11, 1993.

IT IS FURTHER ORDERED that the City of Riverside's cancellation of the Agreement dated January 18, 1991 between the Debtor and the City of Riverside (the "Agreement") is not void and that the cancellation was not affected in any manner by the automatic stay.

IT IS FURTHER ORDERED that the City of Riverside's request that the police and regulatory power exception to the automatic stay contained in 11 U.S.C. § 362(b) (4) be applied to the City of Riverside's cancellation of the Agreement is denied.

IT IS FURTHER ORDERED that the City of Riverside's request for attorneys' fees is denied.

DATED: February 07, 1996

/s/ John J. Wilson
JOHN J. WILSON
UNITED STATES
BANKRUPTCY JUDGE

APPROVED AS TO FORM AND CONTENT:

RUS, MILIBAND, WILLIAMS & SMITH
A Professional Corporation

By: /s/ John J. Williams
J. SCOTT WILLIAMS
Attorneys for Movant,
CITY OF RIVERSIDE

LAW OFFICES OF WILLIAM M. BURD

By: /s/ William M. Burd

WILLLIAM M. BURD
Attorneys for Debtor,
NATIONAL ENVIRONMENTAL
WASTE CORPORATION

In re: NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California Corporation Debtor.	Chapter 11 Case No. SA93-14825 JW

NOTICE OF ENTRY OF JUDGMENT OR ORDER AND CERTIFICATE OF MAILING

TO ALL PARTIES IN INTEREST ON THE ATTACHED SERVICE LIST:

1. You are hereby notified, pursuant to Local Bankruptcy Rule 116(1)(a)(IV), that a judgment or order entitled *(specify)*:

Order (1) granting motion to annul automatic stay for cause and (2) denying motion for order determining police and regulatory power exception to automatic stay applicable to actions taken by the City of Riverside re Solid Waste Collection

was entered on *(specify date)*: February 09, 1996

2. I hereby certify that I mailed a copy of this notice and a true copy of the order or judgment to the persons and entities on the attached service list on *(specify date)*: February 09, 1996

Dated: February 09, 1996

JON D. CERETTO
Clerk of the Bankruptcy Court

By: /s/ John Craig
Deputy Clerk

SERVICE LIST

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INTERNATIONAL RUBBISH
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APPENDIX D

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

In re: NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation, Debtor.	FILED January 6, 1998 Cathy A. Catterson, Clerk U.S. Court of Appeals No. 96-55825 DC No. CV 96-299 LHM
NATIONAL ENVIRONMENTAL WASTE CORP., a California corporation, Appellant, v. CITY OF RIVERSIDE, a political Subdivision of the State of California, Appellee,	ORDER

Before: REIHNHARDT and TASHIMA, Circuit Judges, and SHADHUR, District Judge.*

The Panel has voted to deny the petition for rehearing. Judges Reinhardt and Tashima have voted to reject the suggestion for rehearing en banc and Judge Shadur so recommends.

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* The Honorable Milton I. Shadur, Senior United States District Judge for the Northern District of Illinois, sitting by designation.

The full court has been advised of the suggestion for rehearing en banc, and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35 (b).

The petition for rehearing is denied and the suggestion for rehearing en banc is rejected.

APPENDIX E

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES - GENERAL

Case No. SA CV 96 – 299 – LHM Date: 4/29/96

Title In re National Environmental Waste Corporation

DOCKET ENTRY

PRESENT:

Hon. Linda H. McLaughlin, Judge

Debra Beard, Deputy Clerk
Court Reporter (None Present)

ATTORNEYS PRESENT FOR PLAINTIFFS:
(None Present)

ATTORNEYS PRESENT FOR DEFENDANTS:
(None Present)

PROCEEDINGS:

APPEAL OF ORDER ANNULLING

AUTOMATIC STAY

IN CHAMBERS:

The Court has read and considered appellant's brief, appellee's brief, appellant's reply, and the excerpts of record submitted in connection therewith. Based on the papers

submitted by the parties and applicable law, the Court now rules as follows:

RULING:For the reasons discussed below, the Order of the Bankruptcy Court Annulling the Automatic Stay is AFFIRMED.

(1) Standard of Review. A bankruptcy court's decision to grant retroactive annulment of a stay is reviewed for an abuse of discretion. *In re Kissinger*, 72 F.3d 107, 108 (9th Cir. 1995). A district court reviews a bankruptcy court's factual findings for clear error. *In re Pace*, 67 F.3d 187, 191 (9th Cir. 1995).

(2) Factual Findings. The Bankruptcy Court's order was based on the following findings of fact: (1) The Newco contract required an eight-year notice of termination; (2) Riverside provided such notice on 5/18/93; (3) Newco did not challenge the validity of the notice until 4/10/95; (4) throughout the proceedings, both parties acted on the assumption and belief that Riverside's notice of termination was valid; (5) Newco's actions reinforced the parties' assumption and belief that the Newco contract would terminate in the year 2001; (6) Newco's Reorganization Plan was confirmed based on the validity of Riverside's notice of termination of the Newco contract; (7) Riverside and possibly other parties would suffer sever prejudice if the stay were not annulled; and (8) Newco would suffer no prejudice if the stay were annulled. *See In re National Environmental Waste Corporation ("Newco")*, 191 B.R. 832, 837-38 (Bankr. C.D. Cal. 1996).

The Bankruptcy Court's factual findings are supported by the record. Moreover, Newco offers no evidence or argument to suggest that the findings on which the Bankruptcy Court relied were clearly erroneous. Accordingly, this Court should adopt the factual findings of the Bankruptcy Court. *Pace*, 67 F.3d at 191.

(3) Annulment of the Automatic Stay. A bankruptcy court is required to grant relief from the automatic stay of 11 U.S.C. § 362 (a) for cause. 11 U.S.C. § 362 (d) (1).[1] The debtor has the burden of proof to show that "cause" does not exist. 11 U.S.C. § 362 (g) (2). Retroactive annulment "should be narrow and applied only in extreme circumstances." *In re Shamblin*, 890 F.2d 123, 126 (9th Cir. 1989); *Kissinger*, 72 F.3d at 109.

The "unique facts presented in this case" (*see Newco*, 191 B.R. at 834) support the Bankruptcy Court's order annulling the automatic stay. First, the case presents the unusual circumstance of a contract requiring an 8-year notice of termination (an "Evergreen" contract). Thus, the Newco contract was not terminated prior to the confirmation of Newco's Reorganization Plan and will not be terminated until the year 2001. Moreover, on 5/18/93, Riverside notified, not merely Newco, but each solid waste handler that had entered into an "Evergreen" contract that its contract would be terminated in the year 2001.[2]

Second, although Riverside's notice of termination was given after Newco had filed for bankruptcy, Newco did not contest the validity of such notice until almost two years after it was given. In fact, Newco waited approximately 9½ months after its Reorganization Plan was confirmed to challenge the notice's validity. Such delay in challenging the validity of Riverside's notice may be considered unreasonable. *See Matthews v. Rosene*, 739 F.2d 249, 251 (7th Cir. 1984). Furthermore, although Newco's conduct was

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[1] "Cause" has no clear definition and is determined on a case-by-case basis." *In re Tucson Estates, Inc.*, 912 F.2d 1162, 1166 (9th Cir. 1990).

[2] The reasonableness of Riverside's notice is supported by the Bankruptcy Court's finding that had Riverside applied for relief from the automatic stay to notify Newco of its intent to terminate the Newco contract, the Bankruptcy Court would have routinely granted the motion. *See id.*, at 838.

not egregious, Newco's actions consistently and directly reinforced the parties' understanding that the Newco contract would terminate in the year 2001. *See Newco*, 191 B.R. at 837.

Third, Newco confirmed its Reorganization Plan based on the fact that Riverside's notice of termination was valid. Considering this fact in light of the facts that voiding the notice of termination would cause Riverside to suffer severe prejudice and that annulling the stay has caused Newco to suffer no prejudice, the Bankruptcy Court's finding that it would be inequitable to allow Newco to claim a violation of the stay is not an abuse of discretion. Moreover, not only do the equitable considerations weigh heavily in Riverside's favor, but Newco's actions support the order annulling the stay. *See, e.g., Matthews*, 739 F.2d at 251.

The cases cited by the parties do not address the unusual circumstances of the present case. Nor do they preclude a finding that the present circumstances are extreme. In light of the Bankruptcy Court's careful consideration of the facts and applicable law, this Court finds that the Bankruptcy Court did not abuse its discretion in annulling the stay.

Accordingly, the Order of the Bankruptcy Court Annulling the Automatic Stay is AFFIRMED.

APPENDIX F

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

IN RE NATIONAL ENVIRONMENTAL WASTE CORPORATION, A California corporation, Debtor	No. SA CV 96-299- LHM Bankr. No. SA 93-14825 JW
NATIONAL ENVIRONMENTAL WASTE CORPORATION, A California Corporation, Appellant, v. THE CITY OF RIVERSIDE, a political subdivision of the State of California, Appellee.	ORDER AFFIRMING ORDER OF THE BANKRUPTCY COURT

Based upon the reasons set forth in the Court's Minute Order dated 4/29/96, which is incorporated herein;

IT IS ORDERED that the Bankruptcy Court's Order Annulling the Automatic Stay entered on January 31, 1996 is affirmed.

DATED: 4/29/96

/s/ Linda H. McLAUGHLIN
Linda H. McLAUGHLIN
United States District Judge

APPENDIX G

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In Re: NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California corporation, aka NEWCO, aka NEWCO WASTE, aka NEWCO RECYCLING, Debtor.	)	Case No. SA93-14825-JW Santa Ana, California Wednesday, September 27, 1995 9:30 A.M. Chapter 11
THE CITY OF RIVERSIDE, a political subdivision of the state of California, Movant, vs. NATIONAL ENVIRONMENTAL WASTE CORPORATION, a California corporation, aka NEWCO, aka NEWCO WASTE aka NEWCO RECYCLING, Respondent.	)	Preliminary hrg re motion for relief from stay.

TRANSCRIPT OF PROCEEDINGS
BEFORE THE HONORABLE JOHN J. WILSON
UNITED STATES BANKRUPTCY JUDGE

APPEARANCES:

For Reorganized Debtor:	WILLIAM BURD KAREN SUE NAYLOR Law Offices of William Burd 200 East Sandpointe Suite 620 Santa Ana, CA 92797 (714) 708-3900
For City of Riverside:	J. SCOTT WILLIAMS Rus, Miliband, Williams & Smith 2600 Michelson Drive 7th Floor Irvine, CA 92715 (714) 752-7100
Court Recorder:	CRISTINE HAMILTON U.S. Bankruptcy Court 34 Civic Center Plaza Room 506 Santa Ana, CA 92701 (714) 836-2760
Transcription Service:	V/ARS, Inc. 2001 H Street Sacramento, CA 95814 (916) 448-2457

Proceedings recorded by electronic sound recording.
Transcript produced by transcription service.

[1]

SANTA ANA, CA., WEDNESDAY, SEPTEMBER 27, 1995, 9:30 A.M.

THE COURT: Have a seat, please.
National Environmental Waste, et al.
Appearances, please.

MR. WILLIAMS: Good morning, Your Honor. Scott Williams, of Rus, Miliband, Williams & Smith, for the City of Riverside.

MR. BURD: Good morning, Your Honor. William Burd, appearing on behalf of the reorganized debtor and responding party.

THE COURT: It's your motion, sir.

MR. WILLIAMS: Thank you, Your Honor.

THE COURT: Are the other people here in court here on this matter also?

MR. BURD: Yes, Your Honor. Representatives of my client.

THE COURT: All right. Proceed.

MR. WILLIAMS: Thank you, Your Honor.

Your Honor, this motion was brought essentially in two parts.

First, seeking a determination that the action of the City in terminating the Evergreen portion of the City's contract with NEWCO was a valid exercise of it's police or regulatory power, and therefore an exception to the automatic

[2]

stay under the Bankruptcy Code.

And secondly, if the Court determines that it was not a valid exercise of the police power, a request that the

automatic stay be annulled for cause back to the date of the decision of the City of Riverside City Council in connection with the revocation of the Evergreen portion of its various contracts with city providers.

Your Honor, the case law in support of the contention that this was a valid exercise of police or regulatory powers laid out in the motion.

There has not been in the debtor's opposition a direct challenge to any of the legal reasoning in connection with the action of the City being a valid exercise of its police power; rather, there has been in the debtor's opposition an attempt to shift the focus by alleging that this contract, that the action of the City constituted an effort to control property of the estate under 362(a)(3) rather than the continuation or commencement of an administrative proceeding under (a)(1), and as the Court knows, an (a)(3) action is not excepted by the police power.

As I believe we've indicated in our reply, this is simply — this is simply a red herring. It is clearly not an exercise, by reviewing the legislative history and the relevant case law, clearly this is not an exercise of control over property of the estate and does not fall within

[3]

what the legislative history says the purpose and intent of (a)(3) was. And even — and reviewing the actual language of the contract, it contemplates that the Evergreen portion of the contact, which means the annual perpetual renewal of the eight-year contract, would remain in place until the city council of Riverside reviewed the contract.

So, it is contemplated in the contract that there would be an administrative proceeding that would deal with that issue at some point in the future, because as the way the contract was written, as were all these contracts written, it would essentially go on ad infinitum otherwise.

So, the provision for how the contract was terminated and the contemplation that the Evergreen portion of the contract would be affected by an administrative proceeding is written right into the contract.

So, it is simply inaccurate to try to characterize the City's actions as anything other than the continuation of an administrative proceeding that commenced by pre — by hearings of the city council several months — or by hearings of the various city agencies several months prior to the actual determination by the city council of this issue at the hearing which took place, by happenstance, a few days after the commencement of the NEWCO bankruptcy.

I would also point out, Your Honor, to — just to emphasize that point, to a couple of the cases that we cited

[4]

in our reply.

(Pause)

MR. WILLIAMS: The In Re Poule case, which is a 1988 9th Circuit BAP case, is much more analogous to the facts of this case than the case cited by the debtor, the Hillas case, in arguing that this is somehow an (a) (3) action.

In the Hillas case, clearly the efforts of the government in that case were to exercise control over the assets of the debtor because it sought the dissolution of the debtor, the effect of which returned — under Hawaii law returned control of the assets of the debtor to the share-holders. So, the effect of that action was essential; it was to the core of the control of the assets of the debtor. That is not the case with respect to this case.

The action of the city council was an action of the exercise of its police and regulatory powers in making a policy decision that the Evergreen, the perpetual nature of these contracts was not in its best interest and was not good public

policy, and therefore it revoked all of those provisions in all of its contracts.

It was much more analogous to what happened in the Poule case, the 9th Circuit BAP case, where the California Registrar of Contractors revoked the debtor's contractor's license, and that was determined to be a valid exercise of

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police power. That was a policy decision.

Certainly it had an affect on this debtor and it may — and incidentally had an effect on what might be determined an asset of this debtor, which was the license, but it was determined to be an administrative proceeding under (a) (1) and exempt from the police power under (b) (4), exempt from the automatic stay based on the police and regulatory power.

We would submit that in this particular instance, the city council's actions are clearly an exception to the automatic stay, did not violate the automatic stay and constituted a valid exercise of the police or regulatory power.

I could address, if the Court would like, the annulment issues at this time or reserve that until after Mr. Burd has been heard on this issue.

THE COURT: You have the floor, sir.

MR. WILLIAMS: Thank you, Your Honor.

Even if the Court determines that the City's actions were not a valid exercise of the police or regulatory power, we believe that cause exists to annul the automatic stay to ratify the City's actions in this regard.

Essentially, Your Honor, this action took place — had been the continuation of a proceeding which commenced several months prior to the filing of the NEWCO bankruptcy,

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which was based on a completely different set of facts.

The City always considered this to be a police power action and did not at any point consider what it had done to be a violation of the automatic stay.

The debtor argues that this action, assuming that it's not a valid police power action, is void ab initio, and that that's clear, it is void, and that they have no duty whatsoever to advise the City that it considered the City's actions void so that the City could somehow do something else, get relief from stay or whatever, and has cited various cases in that regard.

They do, however, admit and concede that where the debtor's actions have been so-called stealthily silent, such that they have allowed the other party to continue on the road without knowledge that their actions were void by virtue of the automatic stay, that that would constitute cause for annulment of the automatic stay; that it's an estoppel argument, and that estoppel constitutes cause for annulment of the automatic stay.

What we have here, Your Honor, is a situation where although the City was aware of the bankruptcy filing, it was not aware of the fact that its actions violated the automatic stay because it believed its actions were not subject to the automatic stay because they were police power actions.

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Now, what happened after that. We had three instances which we've cited in our pleadings.

One instance where the debtor did notify the City that it considered an action to be a violation of the automatic stay, the City conformed its actions accordingly.

Secondly, we had a pleading in connection with the process of reorganization of the debtor in which the debtor's

court-appointed accountant replied to arguments about the feasibility of the case by saying, well, yes, it's true that this contract with the City of Riverside, that this Evergreen portion has been revoked, but all that means is that the City has eight whole years before it has to renegotiate that contract with the City of Riverside.

Thirdly, in its plan, in its plan and disclosure statement, the City makes reference to this contract and to the action of the City, and so it has more than implicitly stated its — a position contrary to the position that it takes now that the action of the City was void, and in doing so, it more than remains stealthily silent but acted to affirm the City's position that its actions were not void but were in fact valid and were not subject to the automatic stay because of the exercise of the police and regulatory powers of the city.

And we have cited cases, in fact Judge Fenning's case, also cited by the defendant, which we believe supports

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the position of the City that the actions of the debtor constituted an estoppel and that those actions constitute cause to annul the automatic stay to ratify the actions of the Riverside City Council.

THE COURT: The City could have sought relief from the automatic stay at any time during the bankruptcy proceedings, isn't that true?

MR. WILLIAMS: It certainly could have, Your Honor.

THE COURT: And the City could have given a notice, once the plan was confirmed, without any concern about the automatic stay, isn't that true?

MR. WILLIAMS: That is true, Your Honor.

THE COURT: And I suppose the City could have given such a notice that would say, I'm reserving my rights to seek

an order of the Court that the prior notice was valid, something of that nature kind of a —

MR. WILLIAMS: That's correct.

THE COURT: And it chose not to do any of those things.

MR. WILLIAMS: It did not do any of those things, Your Honor, because it never had a moment's thought that its actions in any way violated the automatic stay and the actions of the debtor simply reinforced the City's belief that its actions were correct.

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THE COURT: So, what you're saying is, the City knowingly chose a course of action based upon its perception of the law and was prepared to suffer the consequences if its perception of the law ultimately turned out to be incorrect?

MR. WILLIAMS: Your Honor, certainly the City did not consider the fact that its actions might violate the automatic stay, and in that sense, yes. But did the City go through a thought process in that, gee, I wonder if we might be violating the automatic stay. Ah, I don't think so, let's just go ahead. I don't think that that actually ever occurred. I think it never occurred to the City that this kind of action fell within the context of the automatic stay and might be void.

THE COURT: Well, it's an unusual situation, is it not, where we absolve a person or an entity of the consequences of violating the stay merely because they didn't know the stay was in effect?

MR. WILLIAMS: It is unusual, certainly, and I think the cases cited by both the debtor and us bear that out.

THE COURT: And this case goes even a step farther. This isn't a case of not being aware of the existence of the automatic stay because they're charged with that knowledge, even if they don't know it, and in this

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case, they actually knew of the bankruptcy proceedings, so they're charged, let's say they're double charged with knowledge of the existence of the stay.

I think what you're saying is that even having that knowledge, they determined that they had not — that the stay didn't preclude them from doing what they did, so they did it.

MR. WILLIAMS: Well, —

THE COURT: Is that really what you're saying?

MR. WILLIAMS: Well, Your Honor, there were two actions here.

THE COURT: You know, this isn't the case of an innocent pro per person who bought something at some sort of a sale not aware that there was an automatic stay in effect because the seller was in bankruptcy, this is a case of an entity with legal resources available to it with knowledge of the bankruptcy.

MR. WILLIAMS: There were two actions here. There was the contemplated action of the city council, which occurred simply by happenstance a couple of days after the debtor filed its case. I am not aware of whether the city council or the city attorneys at that — at the time that that city council hearing occurred and the issue of the Evergreen contracts was on its agenda and action was taken, whether they were aware of the NEWCO bankruptcy.

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But certainly I must concede that even if they had not been aware at that time, the notice that came out of that that was ordered by the city council occurred several weeks later and it must be assumed that they were aware of the filing. Certainly they took no action after that to seek relief from stay to be doubly sure, et cetera, et cetera.

But it must be noted that their action was ratified by the debtor, and had the debtor simply said, hey, wait a second, you guys can't do that, we're in bankruptcy. Then they would have said, well, I mean, we don't — we think our actions were a valid exercise of the police power, but if you disagree, we'll get the Court to determine that.

The actions of the debtor, starting with the fact that the debtor's principals participated, both pre- and post-petition in the administrative proceedings relating to the Evergreen contract, would indicate that at no point did the debtor ever disagree and, in fact, affirmatively made statements that agreed with the City's position that this was a valid exercise of police or regulatory power, which we believe —

THE COURT: Am I —

MR. WILLIAMS: — which we believe it is.

THE COURT: Am I correct that the — what we're really talking about here is two years?

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MR. WILLIAMS: That's correct.

THE COURT: Consequences of an adverse ruling to the City is that the debtor gets two more years under the contract, and if the City — so, if the City loses, the debtor gets two extra years, if the City wins, the debtor gets only the eight years that, according to the records, it seems that the debtor anticipated from early on in this proceeding. Is that what we're talking about, a two-year —

MR. WILLIAMS: That's correct, Your Honor.

THE COURT: — a two year extension or no extension? Is that it?

MR. WILLIAMS: That's correct, Your Honor.

THE COURT: All right. Thank you.

Mr. Burd.

MR. BURD: Your Honor, the problem with the City's police and regulatory power argument is that it totally ignores controlling 9th Circuit law.

The act at issue here was the act of the City in cancelling a contract with the debtor, sending a notice of termination of the contract.

THE COURT: It really wasn't a cancellation of the contract.

MR. BURD: Well, a notice that the contract would terminate in accordance with the provisions of the contract.

The 9th Circuit has, in a number of cases,

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considered the question of the affect of the automatic stay on a debtor's contractual rights. One of the cases is the *In Re Minoco Group of Companies*, cited in our moving papers, which deals with an insurance contract. Another case is a 9th Circuit decision in *In Re Computer Communications, Inc.*, also cited in our papers. And the third 9th Circuit decision is the case of *In Re Carroll*, likewise cited in our responsive papers.

In all three of those cases, the 9th Circuit Court of Appeals held that an action to terminate a contract after the filing of a bankruptcy petition violates 11 USC Section 362(a)(3) as an exercise of control over property of the estate.

The argument by the City that the action itself is contemplated by the contract and that therefore it somehow should be excepted from the scope of 362(a)(3) is rather interesting in light of the facts in the Carroll case.

In *In Re Carroll*, a debtor entered into a management contract post-petition. The contract was approved by the

Bankruptcy Court and the contract itself had a termination provision in it providing for termination on 90 days notice.

The other party to that contract subsequently sent that notice while the automatic stay was still in effect. The debtor said, wait a minute, you can't do that without

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getting relief from stay.

And the Bankruptcy Appellate Panel found that the automatic stay did not apply to stay the termination of the management agreement because application of the stay would be in conflict with the Bankruptcy Court order approving the management agreement which provided for termination upon 90 days notice.

The 9th Circuit reversed. The 9th Circuit held that the debtor's contractual rights, the contract was property of the estate and that it could only be terminated and that the termination violated 362 (a) (3) and that the other party to the contract was required to get relief from stay prior to terminating the contract.

The case is extremely analogous to the case at bar. There is a provision in the contract which provides for sending notice of termination. All the City had to do was get relief from stay to do it.

The City admits that there is no police or regulatory power exception to 11 USC Section 362(a)(3), and every case in which the 9th Circuit has considered contractual relations of a debtor, the 9th Circuit has consistently held that the debtor's contracts are protected by 362 (a) (3). That being the case, the police or regulatory power exception asserted by the City in this case is a nonissue.

In addition, the legislative history of the police

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and regulatory power exception indicates clearly that it was not the intent that that exception should apply to the contractual rights of a governmental agency.

A case called *In Re University Medical Center*, also cited in our papers, the 3rd Circuit explained it as follows:

> "Government agencies are only excepted from the reach of the automatic stay when proceeding to enforce such governmental units' police or regulatory powers." 11 USC 362(b). Congress intended this exception to apply where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety or similar police or regulatory laws, or attempting to fix damages for violations of such law. Neither the language of Section 362(b) nor its legislative history indicates that this exception was intended to permit government agencies to enforce contractual rights against a debtor without first seeking relief from the automatic stay."

Every case, every case cited by the City in

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support of its argument that its actions are somehow subject to the police or regulatory power exception involve an action by an administrative agency against a debtor accused of violating the law. Every case.

There is not a single case where a governmental entity has terminated a contract based on no allegation of violations of the law by the debtor, but simply in accordance with the provisions of the contract. In other words, acting in a normal commercial manner, which is what the City was doing here, no different than any other party to a contract.

There is no case where a Court has found that such action is subject to the police or governmental powers exception.

Turning to the request to annul the stay.

The City seems to gloss over or ignore the fact that in every case cited by them in support of their request for annulment, the debtor actively concealed the fact of the bankruptcy.

In this case they admit that they were aware of the bankruptcy proceeding. It is, I think, black letter law throughout the country, certainly in the 9th Circuit, that knowledge of the bankruptcy proceeding is the legal equivalent of knowledge of the automatic stay.

There is one case I believe cited

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by the City where the creditor was in fact aware of the bankruptcy proceeding. However, in that case, the litigation was instituted by the debtor and the other party cross-complained. The debtor did not even assert the automatic stay until after an adverse judgment had been entered against him on the cross-complaint, in fact, it was three years after the adverse judgment was entered against him, and the creditor was taking enforcement action.

And at that point, I believe it was the 7th Circuit said, wait a minute. You led this person down the primrose path and you've waited too long, and the creditor would be severely prejudiced if we were now to undue basically seven years of litigation.

In every other case, the party was truly an innocent party without knowledge of the filing of the bankruptcy.

The estoppel argument, which is really raised in the reply, Your Honor, at page 7 of the reply, the City asserts, and I quote,

> "Estoppel applies where a party has taken inconsistent positions or has remained silent in the face of a duty to speak."

That's an incorrect statement of the law; I'll get to that in a minute.

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First, the debtor has not taken an inconsistent position. The City argues that a declaration by Chris Reehl, who is a professional accountant employed by the debtor to testify regarding feasibility of the debtor's plan at the confirmation hearing, somehow constitutes an admission by the debtor of the legality of the City's acts.

One, I think only this Court can pass on the legality of the City's act, I'm not sure that the debtor's opinion really means anything unless somehow the City was misled.

Secondly, Mr. Reehl is not an authorized spokesperson for the debtor. He was an expert witness employed by the debtor to testify regarding feasibility.

As far as the debtor's disclosure statement itself, if you look at the language, it is simply a neutral factual recitation of what transpired; the city council met, the city council sent the letter. There is no conclusion drawn and the City — or the debtor does not acknowledge anything.

Assuming for the sake of argument that the debtor has taken inconsistent positions, that's not enough for equitable estoppel. The City cites the decision of Judge Fenning in *In Re Ronan* in support of its statement that estoppel applies where a party has taken inconsistent positions or has remained silent in the face of a duty to

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speak. In fact, what the decision says is the following, and this is at page 485, that:

> "The four essential elements of equitable estoppel are: (1) the party to be estopped must know the facts; (2) he must intend that his conduct shall be acted on or must so act that the party asserting the estoppel has a right to believe it is so intended; (3) the latter must be ignorant of the true facts."

Not the latter must be ignorant of the law, but the latter must be ignorant of the true facts. The City was not ignorant of the facts. The City was aware of the bankruptcy proceeding.

And finally,

> "He must rely on the former's conduct to his injury."

The City has presented no evidence whatsoever that it relied on anything that the debtor did, or that it has in any way been injured by anything that the debtor did, assuming it could get around the problem that it has with the actual knowledge of the bankruptcy proceeding.

Finally regarding annulment, the 9th Circuit has consistently held that it is an extreme remedy to be used

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sparingly. And in *In Re Schwartz*, in reversing the Bankruptcy Appellate Panel, the 9th Circuit Court of Appeals in voiding an assessment made by the Internal Revenue Service three years prior in an earlier bankruptcy case, stated simply, we will not reward those who violate the automatic stay.

I think based on the overwhelming 9th Circuit authority, Your Honor, the City's motion should be denied in all respects.

THE COURT: Mr. Burd, with regard to the annulment argument, if the facts were, and I'm going to pose to you a partial hypothetical and a partial nonhypothetical situation, let's assume that the disclosure statement and the projections contained therein were based upon the debtor's belief and assumption that the contracts would terminate eight years out from the City's notice.

Let's assume that the resolution of the disputes with really the only creditor of consequence in this case which established a payout period in an amount for the satisfaction of the judgment, should that judgment ultimately be affirmed on appeal, all were based upon calculations that a — wherein the debtor assumed the contract would terminate eight years from the notice.

If the disclosure statement provided for it, the plan provided for it, at all times in presenting to this

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Court evidence of the feasibility of the plan and of its ability to make the payments contemplated by the plan, the eight-year-from-notice date was the basis for making those calculations. I suggest to you that those are facts and not hypotheticals.

And let's further assume that on many occasions the debtor and its principal, in that case the debtors and Mr. Cardelucci, repeatedly made statements to the effect that the contract would terminate eight years out, that had an impact on the ability of the debtor to make the payments — to confirm a plan. All of that, I think, is part of the record.

And let's further assume, and what I'm about to say is not part of the record, let's further assume that the debtor, either through its own knowledge or on advice of counsel, well knew that it had another potential ace in its hand; to wit, the City's notice may well have been violative of the stay and void, which could give it a — as long as the City slept on its

rights, it would get more time in the future, it might get more time on the contract in the future. Let's assume that the debtor knew that, consciously knew that, would that, in your opinion, be sufficient to raise an estoppel against the debtor or justify the Court annulling the stay?

MR. BURD: Your Honor, before I respond to that,

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if I may, I would respectfully disagree with the Court's characterization that the first part of the scenario fits the facts in this case, because it does not. The debtor consistently said we don't know what's going to happen.

THE COURT: Oh, there's no question about that, and nor does the debtor know now, nor would the debtor know if the City had got relief from the stay, or if the notice was valid for any other reason; the debtor still says I don't know because they routinely terminate these contracts and then renegotiate them. And, in fact, the notice in this case says they may be renegotiated.

So, there is always that element of uncertainty in the future, so we all know that. But I'm asking you to assume what I think the facts are, that the debtor's entire reorganization was based upon the assumption that the contracts might terminate eight years out from the notice.

MR. BURD: Your Honor, even if we were to assume that all that is correct, it would seem to me that under the four essential elements of equitable estoppel set forth in the Ronan decision, there is one critical problem for the City, and that is that one of the requirements is that the latter must be ignorant of the true facts.

If the fact is that they were aware of the bankruptcy then, as a matter of law, they were aware of the automatic stay and they cannot then be said to be ignorant

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of the true facts.

Secondly, they have presented no evidence whatsoever that they relied on anything that the debtor did, or in the Court's scenario, there is no supposition that the City somehow relied on anything to its detriment or that it has suffered any injury.

And those are two essential elements, based on the Ronan decision, of equitable estoppel.

THE COURT: Now, turning to the first part of the City's argument and your argument.

First, should it make a difference in determining whether the stay, whether the contract was property of the estate for purposes of the decision in this case, should it make a difference that we are dealing here with a notice of termination that says eight years from now the contract will terminate? Whereas, in the Carroll case it was a 90-day notice, in the infamous Computer Communications case, it was 60 days notice, and we're now dealing with a eight-year notice, should that make a difference?

MR. BURD: Your Honor, I don't know whether it should or not, but it does seem clear that 362(a)(3) prohibits the exercise of control over property of the estate.

THE COURT: No one questions that. What about the license cases? Suppose the party — suppose the debtor has a license to do something, and by all normal standard's, the

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license is property of the estate, it's an asset, it has value, and the governmental agency terminates the license without getting relief from automatic stay.

Now, we have what I suggest is this somewhat of a basic inconsistency. You say that because the contract is an asset

of the estate or is property of the estate, therefore (a) (3) applies. At the same time, I think you say, I think you concede that the — and if you don't concede it, I would certainly so rule, that the conduct of the city council in conducting a meeting, putting a matter an the agenda, giving notice and doing all of those things of an action it's going to take, is clearly an exercise of the police power.

It would be ludicrous if the City came in here and asked for relief from stay in order to conduct a hearing on whether or not Evergreen contracts should be terminated in the exercise of its powers with relation to waste disposal in the city.

And I think even you concede, if I read through the papers carefully, I think even you concede or certainly don't oppose the concept that what the city council did prior to giving the notice was an exercise of police power.

MR. BURD: Your Honor, I don't concede that it was an exercise of police power within the meaning of 365(b) (4) (sic). It was certainly clearly within the power of the

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city council to manage the affairs of the city.

THE COURT: And it doesn't —

MR. BURD: But in this case, it —

THE COURT: Doesn't dealing with waste disposal come under the rubric of managing the affairs of the city?

MR. BURD: Your Honor, what the public — yes, it clearly does, Your Honor. The question is whether that also constitutes an exercise of police power within the meaning of 362(b) (4), and I would respectfully submit it does not.

THE COURT: Well, but I'm not talking about (b) (4), I'm talking, really, about (a) (1), the commencement or continuation of a judicial administrative or other action or

proceeding that was or could have — against the debtor that was or could have been commenced before the commencement of the action.

MR. BURD: Your Honor, I would question whether—

THE COURT: And (b)(4) says, "Under subsection (a)(1) of this section, the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power."

Now, are you really arguing that convening the city council to deal with Evergreen contracts involving

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waste disposal is not a valid exercise of the governmental unit's police or regulatory power?

MR. BURD: The question is whether it's within the meaning of Section (b) (4), Your Honor.

THE COURT: And you're suggesting it's not?

MR. BURD: I am suggesting — I am suggesting in this case that the action does not fall within the ambit of (b)(4), yes, Your Honor.

THE COURT: In other words, what you're saying is that the City must come to court and ask for the stay to be lifted in order to convene the city council and to place on the agenda the — any matters relating to waste, the control of waste or the disposal of waste within the city?

MR. BURD: No. I am not suggesting that at all, Your Honor.

THE COURT: Sounds like you are.

MR. BURD: I am suggesting that they are required to obtain relief from stay in order to terminate the contract.

THE COURT: Ah, but now you've — now you've you neatly slide over there. I'm not there yet, Mr. Burd. Where I

am is at the point of the City initiating the action which led up to giving the notice, but prior to giving the notice. Is that, from your judgment, not governmental police or regulatory power, exercising it?

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MR. BURD: If we're speaking in the abstract, yes. I mean, I think it is —

THE COURT: I don't think we are speaking in the abstract —

MR. BURD: Oh, —

THE COURT: — because it was done here.

MR.,BURD: Well, Your Honor, we have to go back to the contract itself and the provision —

THE COURT: Get away from the contract, Mr. Burd. I concede, for purposes of our brief little discussion, that a contract is property of the estate. I would like you to concede, and if you don't feel comfortable doing it, I guess you won't, that the steps taken by the City, up to but not including issuing the notice of termination were a valid exercise of the police power.

MR. BURD: I would assume that it is, Your Honor. I mean, —

THE COURT: You're assuming.

MR. BURD: Yeah.

THE COURT: You don't —

MR. BURD: Your Honor, I'm not an expert on government law. I mean, —

THE COURT: But, so you don't — you don't contend in this case that it was not a valid exercise of the police power.

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MR. BURD: I contend in this case that it was not an exercise of police power —

THE COURT: What was not?

MR. BURD: —within the meaning of Section (b)(4).

THE COURT: What was not? Let's start out with what probably happened. Some kind of — somebody put something on the agenda of the city council, if that's the body that does that, and at some point, the agenda gets published and maybe notice gets sent out to the entire community, I don't know what gets done, but you can anticipate certain actions taken by a city relating to putting matters on the agenda, one of which would be the possible termination or issuing a notice of termination of Evergreen contracts.

Now, is all of that stuff covered by the automatic stay so that the City couldn't even do that?

MR. BURD: As to NEWCO in this case, I think it would be, Your Honor, because that's the very act that terminated the contract.

THE COURT: No, that's not the act that —

MR. BURD: In other words, the city council vote.

THE COURT: The contract has not been terminated. The only thing that's been done is a notice has been given.

MR. BURD: Of termination.

THE COURT: Eight years from now, the contract may

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be terminated, but right now, I have a vision of the city council conducting maybe public hearings or private hearings, I don't know what they do, but I have a vision of doing what cities and city councils do, and I have an extreme

problem in saying that is not an exercise of the governmental police or regulatory power.

MR. BURD: Your Honor, when the —

THE COURT: But you won't — look, you don't have to agree with me, so you won't concede that. And from that, I take what you're saying is that nothing that the City did in connection — which ultimately resulted in giving the notice was an exercise of the police power under (b) (4).

MR. BURD: Well, you see, Your Honor, the problem is the notice itself. Under the contract, it's the vote of the city council, the city council deciding that the contracts will be terminated in eight years that accomplishes that, and under the contract, they're required to send notice to the haulers within 10 days of taking that action. So, presumably the city council's actions wouldn't be effective if the notice wasn't sent. But it's not the sending of the notice that effects the termination eight years hence.

THE COURT: It isn't? Is it the vote of the city council?

MR. BURD: That's what the contract says.

THE COURT: Even if no notice is send?

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MR. BURD: No, Your Honor. I think that would vitiate the vote. If notice were not sent, I think the haulers could argue that the vote is vitiated, but it's the actual — no, without the vote of the city council, the notice couldn't be sent.

THE COURT: Well, we have other matters on the calendar.

It occurs to me, Mr. Burd, that what — the real problem here is this: (a)(3) clearly provides that the stay covers any act to exercise control over property of the estate.

The cases are clear that a contract or contract rights that the debtor has are property of the estate. (a)(4) says, we

exclude under (a)(1) any governmental action, including the commencement or continuation to enforce the unit's police or regulatory power. (a) (1) says the commencement or continuation, including — and I'm paraphrasing, judicial administrative, or other action or proceeding against the debtor, et cetera, et cetera.

If you read (a)(4) and (a)(1), the question you ask is, was the actions of the City, or were the actions of the City an exercise of their governmental police or regulatory power, and I suggest to you that certainly some of them were.

(a)(3) says, again to paraphrase, anyone seeking

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to exercise control over property of the estate is subject to the stay. The contract rights that the debtor has clearly are property of the estate.

And finally, issuing the notice of termination, I suggest, might well be construed to be the continuation of action or proceedings by a governmental unit to enforce the police or regulatory power.

So, under the facts of this case, it seems to me, we have perhaps a sharp contrast, indeed, a conflict between (a)(3) on the one hand and (a)(4) — or (b)(4) and (a)(1) on the other hand, because we have what I suggest to you is both actions and continuations of actions of a valid exercise of the police power, and the continuation of those actions clearly are exercise of control over property of the estate.

Of course, it's not unusual for the Bankruptcy Code to contain conflicting provisions, as we all know, but I think that's where the rub is in this case. And that's why I go back to the original - one of the original questions I asked you is, is the fact that the cases, the 9th Circuit cases that set out this law that supports your position pretty clearly, Carroll and CCI, deal with 60 and 90-day notices, and this one deals with an eight-year notice, should that make a difference.

MR. BURD: I —

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THE COURT: In any event, I have other matters on calendar. This matter is taken under submission.

Thank you all.

MR. WILLIAMS: Thank you, Your Honor.

MR. BURD: Thank you, Your Honor.

(Pause)

THE COURT: Oh, by the way, Mr. Burd, do you agree, as I think Mr. Williams did, that the impact of all of this, whatever the outcome is, is about two years difference between eight years out from the notice and 10 years from the decision? Is that —

MR. BURD: Well, —

THE COURT: Is that really what — the monetary and the practical impact of the decision here?

MR. BURD: Yes, Your Honor, assuming that mean, if the Court were to rule in the debtor's favor, then assuming the city council acts expeditiously to send the notice properly, then, yeah, we're talking about the contract running two years.

THE COURT: Talking about two, two more years.

Thank you.

MR. BURD: Thank you, Your Honor.

MR. WILLIAMS: Thank you, Your Honor.

(Whereupon, the hearing was adjourned.)

CERTIFICATE

I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

/s/ Gwen J. Van Every June 8, 1996
Gwen J. Van Every, Transcriber

APPENDIX H

ARTICLE III
BACKGROUND OF DEBTOR
AND SIGNIFICANT PRE-PETITION EVENTS

A. Description of Debtor's Business

1. NEWCO

NEWCO is a private rubbish hauler for the City of Riverside, California (the "City"), with corporate headquarters located at 7000 Jurupa, Riverside, California. NEWCO's Common Stock is owned 100% by Mr. Sam Cardelucci ("Cardelucci"). Cardelucci is also a debtor in a Chapter 11 proceeding, Case No. SA 93-14797 JW filed on May 3, 1993.

For purposes of rubbish collection, the City is divided into five "areas", four of which are currently serviced by NEWCO. An area is a geographically defined territory within the City. Each area, in turn, is divided into "commercial/industrial" and "residential" type customers. A private rubbish hauler may have either exclusive or non-exclusive rights to service each type of customer.

The rights to service such customers are granted by the City pursuant to contracts (and extensions thereof) negotiated with the private rubbish haulers. NEWCO's specific rights are enumerated in that certain contract with the City dated January 18, 1991, a copy of which is attached hereto as Exhibit "B". NEWCO has an estimated 70% market share in the City.

2. IRS

IRS is a private rubbish hauler for the County of Riverside, California (the "County") , with corporate headquarters located at 7000 Jurupa, Riverside, California. IRS's common stock is 100% owned by Cardelucci.

For purposes of rubbish collection, the County is divided into seven operating "zones". A zone is a geographically defined territory within the County where garbage haulers operate under a permit obtained from the County which is renewable on an annual basis. Customers are divided into residential and commercial/industrial in similar fashion to the city of Riverside. IRS operates in two of the seven zones which are within an approximate radius of 25 miles from the corporate facility and derives most of its revenues from residential customers.

The County itself does not participate in garbage collection and utilizes only private haulers. All districts except for one do not have exclusive hauling rights and are open to competition. IRS competes mainly with Edco (formerly Trico) in its two zones and, overall, has a relatively low market share in the County due to its small geographical coverage.

IRS' business is obtained mainly through advertising (e.g. Pennysaver) and word of mouth.

B. History of Debtor

1. NEWCO

In 1967, Cardelucci and Mr. John O'Leary formed O'Leary Disposal, Inc. ("ODI"). In or about October, 1967, ODI obtained the exclusive commercial/industrial refuse contract for a portion of the City by being the lowest bidder. The contract, which

commenced in or about July, 1968, was initially for a five-year term with a five-year renewal option.

In 1972, Cardelucci acquired 100% ownership of ODI and in 1975 changed the name of the company to National Environmental Waste Corporation - the current name of the Debtor.

NEWCO's primary source of revenue is and always has been its contract with the City. Notwithstanding a long history of political battles with City officials wherein NEWCO has had to continuously assert its rights under its contract, NEWCO has experienced significant success by having its contract with the City extended several times. Such extensions culminated in 1984 with NEWCO receiving a self-renewing contract which began in 1991. This contract is renewed automatically each year for an eight-year term unless otherwise terminated.

NEWCO also receives revenue from the rental of a 100% owned condominium located at 69425 N. Avenida De Las Mon, Cathedral City, CA 92234. The condominium rent is $900.00 per month and the tenant is current. Neither the tenant nor the ground lessor are insiders of NEWCO or IRS.

NEWCO has grown from 8-employees and 5 trucks in 1968 to 86 employees and 44 trucks in 1993. NEWCO's growth has been mainly attributable to the population growth in the areas which it services. NEWCO believes that its success, in no small measure, is also due to its perseverance in asserting its rights under its contract with the City. NEWCO has also expanded its business through the purchase of additional areas. NEWCO's initial contract in 1968 (operating as ODI) was for commercial/industrial rubbish hauling in Area I. In 1985, NEWCO received the rights to commercial/industrial and residential

rubbish hauling for Area V from the city. In 1986, NEWCO received the commercial/industrial rubbish hauling rights for Area II and purchased the commercial/industrial and residential rights to Area III from CYRS Disposal. The City currently services the residential customers in Areas I and II. NEWCO is not authorized any activity in Area IV. As mentioned above, this geographical coverage provides NEWCO with an approximate 70% share of the market.

Current contract disputes include the rights to haul rubbish for apartment buildings in Areas I and II. Although rubbish hauling for apartment buildings has been redefined to be commercial/industrial and within NEWCO's service area, the City continues to haul rubbish for several apartments in these areas. In addition, issues have arisen concerning the billing of customers. From 1984 until 1991, the City billed the customers and experienced significant write-offs. Such write-offs were charged to NEWCO. In 1991, NEWCO was successful in securing the right to perform its own billing and thereby has minimized the write-offs

Area exclusivity is a continuing problem with outside contractors offering services to NEWCO's customers. NEWCO continues to experience difficulties with City officials failing to enforce the exclusivity provisions of the contract.

On May 11, 1993 the City Council of the City of Riverside approved a recommendation to provide the required eight-year notice to the private refuse haulers (including NEWCO) to terminate their contracts. In a letter dated May 18, 1993, NEWCO received written notice from the City's Public Works Director that its

contract with the City will expire on May 11, 2001 (copy attached hereto as Exhibit "C").

2. IRS

IRS was formed in 1986 to provide rubbish hauling services to the County of Riverside. IRS's expertise in the rubbish hauling business is a direct extension of the involvement of its sister company, NEWCO, which has been a private rubbish hauler for the City of Riverside for over 20 years. IRS also utilizes trucks, equipment and corporate services provided by NEWCO, for which it is charged a management overhead allocation. IRS also contracts for employee services from NEWCO.

IRS' growth has been mainly attributable to high levels of real estate construction in the County and improved penetration of the customer base. Without exclusive contracts, competition is

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